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March 19th, 2011



Politics this week



Japan's government struggled to contain an unfolding nuclear disaster at its Fukushima Dai-ichi power complex, about 240 kilometres (150 miles) north-east of Tokyo. After an earthquake of magnitude 9.0, the biggest in Japan's modern history, and the devastating tsunami it triggered, at least four of the complex's six reactors suffered damage, and there was some leakage of radiation. Radiation levels around the plant at times rose sharply, leading at one point to the evacuation of workers trying to control the disaster. See article

The number of dead and missing after the **earthquake and tsunami** stood at more than 14,000 by mid-week and was expected to climb. Around 500,000 people were rendered homeless and endured desperate conditions in temporary shelters, with no electricity and freezing weather.

A number of foreign embassies and firms withdrew their personnel from **Tokyo**. But the government insisted that the 35m people in the Tokyo area faced no immediate health threat. Emperor Akihito took the extraordinary step of appearing on television to express his concern.

The disaster in Japan revived German concerns over **nuclear power**. Angela Merkel announced a three-month moratorium on a plan to extend the lifespan of the country's 17 nuclear-power plants, and said that seven facilities built before 1980 would be temporarily shut. The European Union announced plans to test the safety of all nuclear plants in the 27 member states and China suspended approvals for new nuclear facilities.

Raymond Davis, a CIA contractor arrested in January in Lahore for murdering two local men he said he killed in self-defence, was released by a Pakistani court. Details of the deal that led to his freedom were not made public, but it involved the payment of blood money to the families of the men he killed. The case had led to a serious rift with America, which insisted Mr Davis enjoyed diplomatic immunity and should never have been detained. See article

A Christian serving a life sentence under **Pakistan's** Islamic blasphemy law died in jail in Karachi. Officials said the man had a heart attack, but his family claimed he had been fit and healthy.

The Dalai Lama asked **Tibet's** parliament-in-exile, based in Dharamsala, in northern India, to accept his decision to step down as its leader and devolve his formal authority to an elected politician. He also proposed amendments to the constitution of the exiled government. Many Tibetans were aghast.

At his annual press conference to mark the end of the session of the National People's Congress, **China's** parliament, Wen Jiabao, China's prime minister, renewed his arguments for the importance of "political reform". But he did not say what he meant, and rejected comparisons between China and the "jasmine revolutions" in the Middle East. See article

Pleasing to Putin

In elections to regional legislatures in **Russia**, United Russia, the pro-Kremlin party, swept the board. But in several regions it took fewer votes than some observers had expected. The Communists finished a distant second. See article

In a television interview, Saif al-Islam Qaddafi, son of the Libyan ruler, said that his father's regime had helped fund **Nicolas Sarkozy's** 2007 presidential election campaign. However, he provided no evidence for the claim and a spokesman for the president issued a denial.

Cracking down



Forces loyal to Muammar Qaddafi won control of rebel towns in **Libya's** east and west. Western powers discussed the imposition of a no-fly zone to protect civilians. The Arab League endorsed such a move, so did Britain and France. America gradually moved towards that camp, but Russia and others voiced doubts. See article

The embattled government in **Bahrain** invited 2,000 troops from Saudi Arabia and the United Arab Emirates on to its soil to help its security forces curb a growing protest movement. After police opened fire on a crowd of mainly Shia demonstrators, the government declared martial law. See article

In **Yemen** protests spread against President Ali Abdullah Saleh but were met with a fierce crackdown. See article

Five members of an **Israeli** family were murdered in a West Bank settlement. The attack was blamed on Palestinian extremists.

In **Niger** Mahamadou Issoufou, a long-time opposition leader, won an election run-off and was declared president.

Harmful to thawing relations

A court in **Cuba** sentenced Alan Gross, an American aid worker, to 15 years in prison. Mr Gross was arrested in December 2009. Cuba's government said he was illegally distributing satellite equipment and accused him of subversion. Meanwhile, Cuba's government devalued the convertible peso by 8% against the dollar. The communist island is suffering a foreign-exchange shortage.

The United States State Department said that Jean-Bertrand Aristide, a former president, should refrain from returning to **Haiti** before a presidential election on March 20th, and that it had asked South Africa, where Mr Aristide has lived in exile since being ousted in 2004, to delay his departure. See article

Mexico's government confirmed a report that it has allowed unmanned American drones to fly over its territory to gather intelligence on drug- traffickers.

Day by day

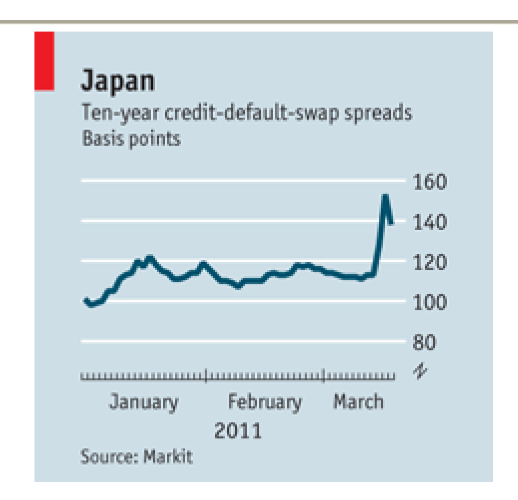


America's Congress looked set to pass another temporary budget measure (the sixth) to fund government services and avoid a **shutdown** of operations, this time until April 8th. But some congressmen grumbled that it would be the last time they support such a compromise. See article

Philip Crowley resigned as the State Department's spokesman, after telling a university audience that the Pentagon's treatment of **Bradley Manning** was "ridiculous and counterproductive and stupid". A soldier, Mr Manning is allegedly behind a mass leak of classified documents to WikiLeaks. He has been held in custody in a military prison and could face

a court-martial. His lawyer has complained about the circumstances of his detention, including being placed on suicide-watch and deprived of clothing at night.

Business this week



Stockmarkets swooned around the world in reaction to the nuclear crisis in **Japan**. In Tokyo the Nikkei index fell by almost 11% in one day. With one of the worst debt positions among industrialised countries, the cost of insuring against default on Japanese sovereign debt soared. Tokyo Electric Power Company, one of the world's biggest energy providers, which operates the stricken Fukushima Dai-ichi nuclear-power facility, saw its share price slump, raising questions about its viability. See article

The ripple effects

Prices fell sharply on a wide range of **commodities** amid worries that the disaster in Japan could hurt trade in East Asia and beyond. But the spot price of **liquefied natural gas** increased when supplies were diverted to Japan to make up for the shortfall in nuclear power. Prices also rose for microchips, as many Japanese manufacturers of the components remained closed.

At a summit in Brussels the leaders of **euro-zone** countries agreed to beef up the bail-out facility for the currency block. Greece won a modest reduction in the interest rate it is paying on its loans, but Ireland received no such concession because it insisted on keeping its low corporate-tax rate. See article

Deutsche Bank revealed that its exposure to risk from sovereign debt in the euro area more than doubled at the end of last year, to euro12 billion ($17 billion), because of its takeover of Postbank. Germany's biggest bank also said it was selling its twin-tower Frankfurt headquarters, dubbed *Soll und Haben* (debit and credit), to a mutual fund for euro600m.

It emerged that regulators in America, Britain and Japan have launched an inquiry into the procedure for setting the London Interbank Offered Rate (**LIBOR**) that banks refer to when making loans to one another. The interest rate is supervised by the British Bankers' Association, which asks a panel of global banks what it would cost them to borrow funds for certain times and in ten currencies. The LIBOR was a gauge of market stress during the financial crisis, but critics argue that the method for setting the rate can be manipulated.

Oh, Renault!

Renault faced a storm of criticism over its botched internal investigation into an alleged case of company espionage. The carmaker sacked three senior executives earlier this year, claiming they had sold information about the company's electric-car business. It apologised to the men this week after French prosecutors found that a crucial piece of evidence had been falsified. Carlos Ghosn, Renault's chief executive, said that he and his chief operating officer, who offered to resign, would forgo their performance bonuses because of the imbroglio.

Warren Buffett's Berkshire Hathaway agreed to buy **Lubrizol**, a specialty-chemical company that produces additives for engine oil, among other things, in a $9.7 billion deal. With $38 billion in cash on hand, analysts expect Mr Buffett's company to make more sizeable acquisitions.

A joint venture formed by Carlyle Group and Tiger Group Investments, which is based in Hong Kong, launched one of the biggest private-equity financing deals to date in **shipping**. The venture will spend more than $5 billion on new container ships and work with Seaspan, an independent lessor, to lease the vessels to Chinese companies. The deal underscores the revival in shipping. Last month, Denmark's Maersk Line ordered at least ten new jumbo-sized container ships.

As expected, **Hewlett-Packard** unveiled plans to expand into cloud-computing services, in which data are stored and run directly from the web. HP has hitherto concentrated on selling the servers on which the data in the cloud are held.

The lingering weakness of America's **housing market** was ever more apparent with the release of data showing that construction starts of new homes had plummeted by 22.5% in February compared with January, the steepest fall since 1984. The number of building permits issued fell to the lowest level in 40 years.

Keep it to yourself

Microsoft released a new version of Internet Explorer, which includes a tracking- protection feature to give users more control over **personal information** that is shared with websites. Meanwhile, the White House threw its weight behind a push to establish tougher rules on the gathering of data on the web in a mooted "privacy bill of rights". See article

PepsiCo announced that it had developed the world's first bottle to be made entirely of a plastic consisting of plant-based materials, which can be fully recycled. Its **"green bottle"** is composed of switch grass, pine bark and corn husk. Pepsi hopes to produce bottles in the future using orange and potato peels and other by-products from food.

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Daily Chart

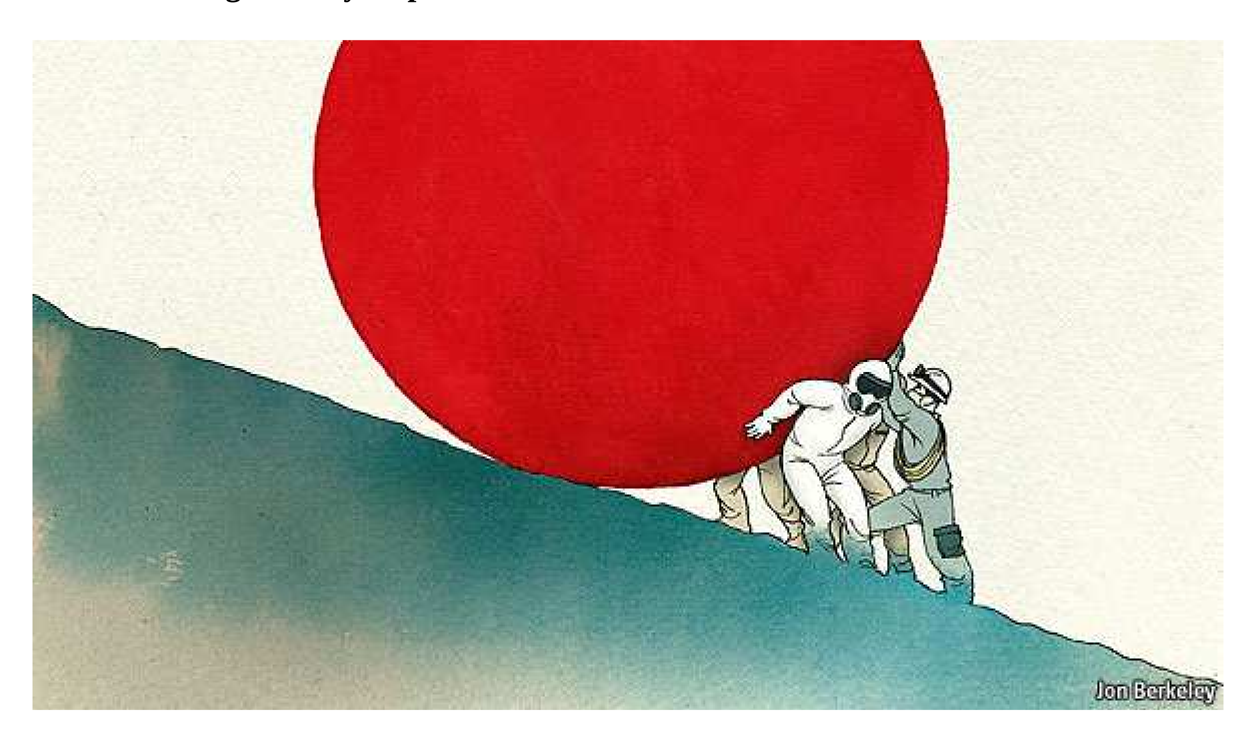
Mar 17th 2011 | From *The Economist* print edition



Japan's hydra-headed disaster

The fallout

Some natural disasters change history. Japan's tsunami could be one



THAT "tsunami" is one of the few Japanese words in global use points to the country's familiarity with natural disaster. But even measured against Japan's painful history, its plight today is miserable. The magnitude-9 earthquake-the largest ever in the country's history, equivalent in power to 30,000 Hiroshimas-was followed by a wave which wiped out whole towns. With news dribbling out from stricken coastal communities, the scale of the horror is still sinking in. The surge of icy water shoved the debris of destroyed towns miles inland, killing most of those too old or too slow to scramble to higher ground (see article). The official death toll of 5,429 will certainly rise. In several towns over half the population has drowned or is missing.

In the face of calamity, a decent people has proved extremely resilient: no looting; very little complaining among the tsunami survivors. In Tokyo people queued patiently to meet their tax deadlines. Everywhere there was a calm determination to conjure a little order out of chaos. Volunteers have rushed to help. The country's Self-Defence Forces, which dithered in response to the Kobe earthquake in 1995, have poured into the stricken area. Naoto Kan, the prime minister, who started the crisis with very low public support, has so far managed to keep a semblance of order in the country, despite a series of calamities that would challenge even the strongest of leaders. The government's inept handling of the Kobe disaster did much to undermine Japan's confidence in itself.

The wider concern

The immediate tragedy may be Japan's; but it also throws up longer-term questions that will eventually affect people all the way round the globe. Stockmarkets stumbled on fears about the impact on the world's third-biggest economy. Japan's central bank seems to have stilled talk of financial panic with huge injections of liquidity. Early estimates of the total damage are somewhat higher than the $100 billion that Kobe cost, but not enough to wreck a rich country. Disruption to electricity supplies will damage growth, and some Asian supply chains are already facing problems; but new infrastructure spending will offset some of the earthquake's drag on growth.

Those calculations could change dramatically if the nuclear crisis worsens. As *The Economist* went to press, helicopters were dropping water to douse overheating nuclear fuel stored at the Fukushima Dai-ichi plant, where there have been explosions, fires and releases of radiation greater, it seems, than the Japanese authorities had admitted. The country's

nuclear industry has a long history of cover-ups and incompetence, and-notwithstanding the heroism of individual workers-the handling of the crisis by TEPCO, the nuclear plant's operator, is sadly in line with its past performance.

Even if the nuclear accident is brought under control swiftly, and the release of radiation turns out not to be large enough to damage public health, this accident will have a huge impact on the nuclear industry, both inside and outside Japan. Germany has already put on hold its politically tricky decision to extend the life of its nuclear plants. America's faltering steps towards new reactors look sure to be set back, not least because new concerns will mean greater costs.

China has announced a pause in its ambitious plans for nuclear growth. With 27 reactors under construction, more than twice as many as any other country, China accounts for almost half the world's current nuclear build-out-and it has plans for 50 more reactors. And in the long term the regime looks unlikely to be much deterred from these plans-and certainly not by its public's opinion, whatever that might be. China has a huge thirst for energy that it will slake from as many wells as it can, with planned big increases in wind power and in gas as well as the nuclear build-out and ever more coal-fired plants.

Thus the great nuclear dilemma. For the best nuclear safety you need not just good planning and good engineering. You need the sort of society that can produce accountability and transparency, one that can build institutions that receive and deserve trust. No nuclear nation has done this as well as one might wish, and Japan's failings may well become more evident. But democracies are better at building such institutions. At the same time, however, democracy makes it much easier for a substantial and implacable minority to make sure things don't happen, and that seems likely to be the case with plans for more nuclear power. Thus nuclear power looks much more likely to spread in societies that are unlikely to ground it in the enduring culture of safety that it needs. China's nearest competitor in the new-build stakes is Russia.

Yet democracies would be wrong to turn their back on nuclear power. It still has the advantages of offering reliable power, a degree of energy security, and no carbon dioxide emissions beyond those incurred in building and supplying the plants. In terms of lives lost it has also boasted, to date, a reasonably good record. Chernobyl's death toll is highly uncertain, but may have reached a few thousand people. China's coal mines certainly kill 2,000-3,000 workers a year, and coal-smogged air there and elsewhere kills many more. It remains a reasonable idea for most rich countries to keep some nuclear power in their portfolio, not least because by maintaining economic and technological stakes in nuclear they will have more standing to insist on high standards for safety and non-proliferation being applied throughout the world. But in the face of panic, of sinister towers of smoke, of invisible and implacable threats, the reasonable course is not an easy one.

Back to Tokyo

No country faces that choice more painfully than Japan, scarred by nuclear energy but also deprived of native alternatives. To abandon nuclear power is to commit the country to massive imports of gas and perhaps coal. To keep it is to face and overcome a national trauma and to accept a small but real risk of another disaster.

Japan's all too frequent experience of calamity suggests that such events are often followed by great change. After the earthquake of 1923, it turned to militarism. After its defeat in the second world war, and the dropping of the atom bombs, it espoused peaceful growth. The Kobe earthquake reinforced Japan's recent turning in on itself.

This new catastrophe seems likely to have a similarly huge impact on the nation's psyche. It may be that the Japanese people's impressive response to disaster, and the rest of the world's awe in the face of their stoicism, restores the self-confidence the country so badly needs. It may be that the failings of its secretive system of governance, exemplified by the shoddy management of its nuclear plants, lead to more demands for political reform. As long as Mr Kan can convince the public that the government's information on radiation is trustworthy, and that it can ease the cold and hunger of tsunami survivors, his hand may be strengthened to further liberalise Japan. Or it may be that things take a darker turn.

The stakes are high. Japan-a despondent country with a dysfunctional political system-badly needs change. It seems just possible that, looking back from a safe distance, Japan's people will regard this dreadful moment not just as a time of death, grief and mourning, but also as a time of rebirth.

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Intervention in the Arab awakening

No illusions

The Arab awakening is succumbing to violence. The outside world has a duty to act

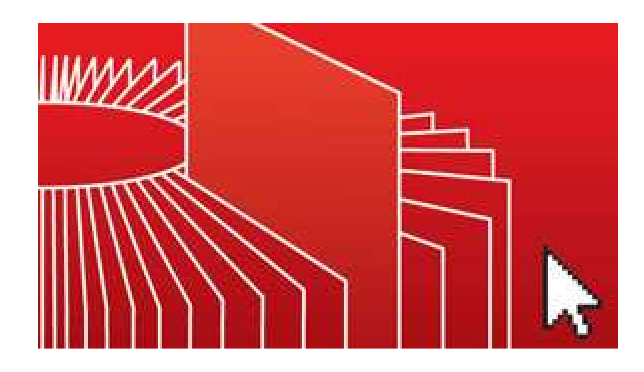


UNTIL the Arab awakening reached Libya, protesters seemed able to prevail armed with little more than self-belief. Not any more. In Bahrain the regime's troops, reinforced by foreigners-mostly Saudis-have stormed the protesters' tent-city at Pearl roundabout, shooting as they went. In Yemen the regime of President Ali Abdullah Saleh has taken to firing live rounds into the crowds. And in Libya itself, as Muammar Qaddafi seizes back the rebel towns strung along the Mediterranean coast, the people are reaping the whirlwind. Torture and death are rampaging through Brega and Zawiya. Terror and despair loom over Tobruk and Benghazi.

As the violence escalates, the outside world no longer has the easy option of simply backing the "reform" of corrupt and oppressive regimes. Instead, it faces hard choices. Are countries content to sit on their hands and watch rebels die? And if they feel they must step in, what exactly can they do?

In Libya, at least, those questions are fast becoming the business of historians rather than policymakers. The moment will soon have passed when a no-fly zone designed to stop Colonel Qaddafi from using his air force could offer civilians much protection. As *The Economist* went to press, the UN Security Council was at last discussing this but Colonel Qaddafi was advancing towards Benghazi (see article). If he arrives at the city, its people will need more than just air cover to save them in what could be a bloody and long-drawn-out battle.

Democracies wisely set obstacles in the way of those who seek to put the world to rights by fighting-however good their motives. Bitter experience in Iraq has taught how liberators soon come to be seen as oppressors. Western troops have found that when they wage war, they own the mess they have created. You cannot fight people into behaving well.



At the same time, democracies shrink from the idea that might is right. After the genocide in Rwanda, nations took on a duty to stop mass-killing if they could. Kosovo, Sierra Leone and Liberia all showed that outsiders can in fact help avert

catastrophes. The Arab awakening is all about human dignity and the rights of ordinary people-values that the West lives by and seeks to promote. For the West to turn its back on Libya's rebels and to stand aside while its allies shoot protesters in Bahrain betrays its own values.

Confronted by the contradictory urges to do good and steer clear, the West has so far accomplished neither. Even as the Arab League and the Gulf Co-operation Council have called for international action against Colonel Qaddafi, the West has temporised and rebel towns have fallen. Europe is at its chaotic worst. France and Britain want a no-fly zone, but Germany, deaf to the pleas of Libyans, sees only risks and entanglement. And in America Barack Obama has summoned up the will to condemn violence and oppression, but, until far too late, studiously avoided summoning up the means to do much about it-a weak stance for a superpower (see Lexington).

Those who wish America to be a force for good will find that disappointing. But those who rejected George Bush's searing and bloody pursuit of democracy should reflect on how they got what they sought.

All talk

No universal formula can cut through the contradiction between values and interests in foreign policy-that is why intervention in Vietnam and Somalia led to neglect in Rwanda, which set the scene for intervention once more in Bosnia and Iraq. And it is why foreign policy is condemned to live with an age-old dilemma. If the West sacrifices its place in the world to its values, then it will be less able to promote them. On the other hand, if the West always puts narrow realpolitik before its values, then its values will be tainted in the eyes of the world.

By that test, the West let down the Bahrainis: sterner talk from Mr Obama may have deterred their attackers. Yet the West does still have options in Libya. To send in Western ground forces would be to own a dysfunctional, violent place. But the West can seize upon Arab backing to help protect eastern Libya. It should jam Colonel Qaddafi's communications and rush in a no-fly zone. If the regime begins to pound Benghazi, then aircraft-including Arab aircraft-should destroy Colonel Qaddafi's tanks, artillery and gunboats.

Have no illusions about the risks of such a policy. Bombing Libyan armour would endanger the lives of pilots and, inevitably, civilians. It would, at least temporarily, partition Libya. The eastern groups under the protection of the outside world may include Islamists and killers who turn out to be just as savage as Colonel Qaddafi. And that is if the policy succeeds.

Even so, these are risks that the West should now take before it is too late. Saving lives in eastern Libya will be hard. Not even trying to save them would be worse.

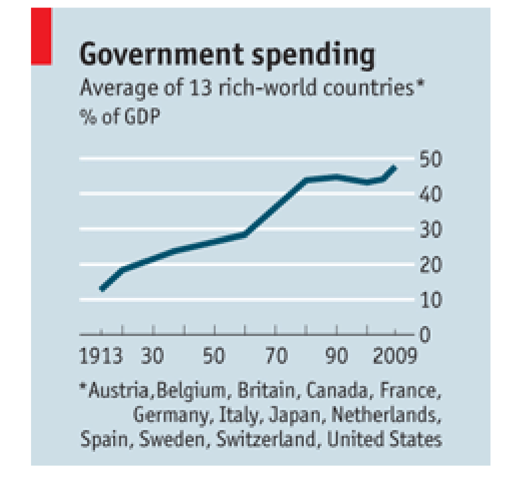
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The ever-growing state

Taming Leviathan

How to slim the state will become the great political issue of our times

"IF SOMETHING cannot go on for ever, it will stop," Herb Stein once observed caustically. The American economist's aphorism has proved apt of late-as applicable to Hosni Mubarak's regime as it was to America's rising property prices. Could it apply to the growth of the state?



Government comes in many shapes and sizes. In some parts of the world, the state is too small. In Guatemala, where the tax take is around a tenth of GDP, private security guards are five times more numerous than the police and army combined. But most of the world has the opposite problem. The state has kept on grabbing an ever larger share of the economy in the rich world for a century (see chart), and the state's regulatory sweep has increased as well.

As our special report this week concludes, the forces driving this growth are powerful-but so are the reasons why it needs to be halted. As a liberal paper, *The Economist* has long favoured a smaller state; but there are pragmatic grounds now for politicians of all sorts to make the state more productive. With ageing populations to care for, many rich-world governments are on course for bankruptcy-unless they raise taxes to levels that would wreck their economies. And emerging markets are watching, keen to cater to the demands of their ever richer citizens-and also to avoid the mistakes of the West.

Behold, the beast changes shape

Attitudes to the big state have swung to and fro, from the liberal attack on patronage in the 19th century to the embrace of the social-democratic consensus after the second world war to Thatcherite privatisation in the 1980s. There are some signs that another rethink is imminent: witness the budget cuts in the euro zone, the battle between Wisconsin's governor and the public-sector unions and David Cameron's "Big Society" rhetoric. There is even the probability that the state's share of GDP may slip back in the short term, as the recovery lifts the overall economy. But many efforts at reform are timid-witness the mendacious budgets produced in Washington by both Barack Obama and the Republicans and their refusal to touch entitlements. If nothing is done other than slimming a few departments, Leviathan will be on the march again.

Why? Because, despite all that rhetoric from the tea-partiers, big government is not just the fault of self-interested bureaucrats and leftist politicians. Conservative voters, even if they don't like taxes, have kept on demanding that the state does more. Just as the left has built hospitals, announced endless programmes to help the poor and indulged the teachers' unions, the right has built prisons, announced wars on drugs and terror, and indulged generals, farmers and policemen. And there are also two structural causes of big government. First, productivity in the state sector, especially in fields like education and health, has lagged behind the private sector. And second, there has been a huge increase in "social transfers", especially benefits for the middle classes and the elderly.

To lose weight, governments have to do two things: learn how to do more with less, which means modernising the state, and cut back on what they offer, which among other things means tackling the social transfers. Both are inevitable, but the first offers the best chance of immediate gains.

Most attempts to "re-engineer" government thus far have fared poorly. But the failures of the current system are getting ever more obvious, especially given the jaw-droppingly large variances in performance. Why should one British health area have eight times more "unscheduled admissions" (the costly sort) than its very similar neighbour? Why should Americans spend twice as much on health as Swedes yet die younger? Each new international education ranking makes it clearer that American schools and continental European universities do not lack money, as unions claim, but need to hire better staff-and be able to sack lousy teachers. Merely bringing the useless bits of the public sector up to something close to average would save a fortune and improve services dramatically. And there are also common themes that emerge time and again: pay good staff well; make performance transparent; simplify taxes (see article); and move towards a small core civil service with a lot of competing suppliers for services.

Public-sector reform is gritty work. Do it well, and a state could provide the same services and benefits for less money. Yet politicians also need to tackle the question of whether the state should be handing out so much to so many. Here politics matters much more, both because voters are more protective of their perks and because there are genuine ideological choices to be made. This paper, for instance, would take an axe to industrial subsidies and to tax breaks (the latter are worth $1 trillion a year in America alone); it would also push up pensionable ages much more quickly than most Western governments are currently doing-and index them to longevity.

The hardest issue of all to tackle will be the perks that currently flow to the middle classes and the elderly. Benefits that were originally designed for the poor have become sops for the middle class; others are going to the elderly for longer than anyone expected. The "all you can eat" buffet nature of European welfare states not only prompts overconsumption; it also means that even those who do well out of the state have little idea how much it is costing overall. Again, the more transparent and modern the state is, the easier it will be to talk about means-testing currently universal benefits.

One fine day

Ideally, the next round of Western elections-especially the presidential one in America-will focus on that. Slimming the state is not an easy conversation. But consider the alternative: an ever fatter state, ever less freedom and ever higher taxes. In the 1990s much was made of the idea that capitalism had got so footloose that states were bound to get slimmer to compete for corporate favours. In fact companies proved more loyal than expected-and the state went on one last splurge. But talent and capital are getting more mobile; and the demographic pressure of those ageing populations is mounting. The ever larger state cannot go on for ever. It will stop.

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Europe's far right

Pause and engage

The best way to stop the populist far right is to counter not pander to its crude message



FROM the tip of Scandinavia to the shores of the Mediterranean, far-right leaders and parties are doing well in opinion polls. Given Europe's history, this has set nerves jangling.

The biggest shock is the rise of Marine Le Pen, leader of France's National Front. Polls put her ahead of both President Nicolas Sarkozy and any likely Socialist challenger in 2012. She will not win the presidency, but she has shed the

jackbooted imagery of her father, Jean-Marie, who shamed France by getting into the run-off against Jacques Chirac in 2002.

The right is on the rise for old reasons and new. Hostility to immigration is sharpened by Islamist terrorism; alienation from the political system is exacerbated by both globalisation and the bail-outs of failing euro-zone countries. Ms Le Pen and her kind trade on anti-Islamist sentiment to resist not just more immigration from north Africa but also Islamification at home. In northern Europe far-right parties play more on hostility to Brussels and the euro. The German government is worried about the possible emergence of a nationalist party pushing to restore the D-mark.

Europe's political establishment has tried many different tactics to defang the far right, none of which has wholly succeeded. The first was to ignore it in the hope that it might go away. Next came a policy of ostracising extremists, throwing a *cordon sanitaire* around parties that won municipal or parliamentary seats. Then came its opposite: embracing the far right and even bringing it into government, in the hope that contact with reality would both moderate it and reduce its appeal.

Mr Sarkozy tried another approach in the run-up to the 2007 election: he occupied the National Front's ground by ranting about immigrants and using coded anti-Islam discourse. A charitable interpretation is that by broadening the respectable right, he left less space for the extremists. Whatever the intent, this strategy had some success in winning back voters. But it is a dangerous path to follow. By espousing the arguments of the far right, the centre may legitimise them; and voters may opt not for the ersatz party but the real thing, especially in a more respectable guise-Ms Le Pen, for instance.

Take them on instead

Mainstream parties would do better to address the extremists head on. Instead of stoking anti-Muslim sentiment by claiming, as Germany's interior minister has, that Islam has no place in a country, explain the importance of integrating minorities. Instead of demonising the Greeks, spell out the arguments for keeping the euro together. Instead of hinting that governments can hold globalisation at bay, explain its benefits and the costs of resisting it. That may sound Panglossian, but it is better than raising voters' expectations only to dash them later. That's what Mr Sarkozy did in 2008 when he pledged to keep a steel plant from shifting production abroad. The jobs went anyway. Little wonder if voters flock to parties that seem to offer a more robust bulwark against painful change.

Dealing with extremists is never easy for moderates, but addressing voters' concerns honestly, and making the argument against the far right stoutly, is the best approach. Those who steal extremists' clothes end up looking too much like them.

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Britain's budget

Osborne's chance

In next week's budget, the chancellor should set out a strategy for radical tax reform



WHEN George Osborne makes his second budget statement as chancellor of the exchequer on March 23rd (see article), he seems set to outline a grand "growth strategy" to counter claims that he is more interested in cutting spending than boosting the economy. But the budget is meant to be about tax-on which, for all its radicalism elsewhere, the government has been timid. Mr Osborne should rectify that.

On the face of it, this is not an ideal time for radical change. Altering the tax system is hard enough when there is spare cash to act as a lubricant. There isn't: although public finances are a bit less dire than Mr Osborne feared when he fashioned his first budget last June, Britain's deficit this financial year will be equivalent to around 10% of GDP. But the scarcity of revenue, though unhelpful, is also a reason for action. An inefficient tax system is a luxury the country might have been able to afford when the economy and tax receipts were healthier. It no longer can. And because reform is politically fraught, and its benefits take time to emerge, a budget in the first year of a parliament offers the best chance to make lasting changes.

First principles

Mr Osborne should set out a strategy for taxes to complement last autumn's bold public-spending plans. A review published in November by the Institute for Fiscal Studies, a think-tank, and headed by Sir James Mirrlees, a Nobel prize-winning tax theorist, sets out some principles that he would be wise to adopt. A good tax system has three main elements: it should be progressive (ie, place a greater burden on the better off); it should not bias choices over how much to work or (with a few exceptions) what to consume; and it should be simple.

The British tax structure, with its thousand-odd reliefs and numerous tax rates, is woefully inefficient. Its complexity imposes costs on business, blunts work incentives and diverts energy from creating wealth to shielding it from tax. The Office of Tax Simplification, a body set up by Mr Osborne last year, has identified 47 tax reliefs that could be easily abolished. But more radical changes are needed to create a system that raises the necessary revenues while doing the least economic harm. The taxation of both savings and property is incoherent and needs rethinking. But having made a modest start in June by cutting the main corporate-tax rate, Mr Osborne should now concentrate his efforts on simplifying personal taxes and broadening the base for VAT.

An ideal system of personal taxation would have a tax-free allowance (so the low-waged pay little or no tax), two or three rates, and a broad base including non-wage income. The current arrangements are far too complex. One absurd kink has been created by the withdrawal of tax-free allowances once income passes pound100,000 ($160,000), leaving a marginal rate of 60% between the middle and top rates of income tax (which kicks in at pound150,001). Alongside income tax is a schedule of national-insurance contributions (NICs), ostensibly a social-insurance levy but in reality an auxiliary wage tax. The two systems are poorly aligned. They should be merged, with the part of NICS paid by employers left as a stand-alone payroll tax.

A single personal-tax schedule with a broad base could ensure the tax system is progressive, which would allow for a complementary broadening of VAT. Only around half of consumer spending is taxed at the standard VAT rate of 20%, a

low share compared with other rich countries. Britain's consumers do not pay VAT on most foods, public transport, children's clothes, banking, books and newspapers. Domestic energy bills attract a 5% rate. Some categories of spending such as food are sheltered from tax to help the poor. But exemptions from VAT distort choices by, in effect, subsidising some consumers over others. They should be scrapped. The revenues raised could be used to compensate those on lower incomes through increased state benefits, a higher tax allowance and rate cuts.

These tax changes could be staged over several years to allow some relaxation of the fiscal squeeze, should the economy falter. Fixing some of the glaring irrationalities in the tax system would have as big an impact on medium-term growth prospects as anything else Mr Osborne is likely to announce in his budget. He should take his chance.

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Hollywood's disc problem

Video nasty

The film business is slumping. It needs to start dealing directly with consumers



IN "THE RING", a Hollywood remake of a Japanese horror film, a videotape has a deadly effect on those who watch it. In reality the opposite is happening: viewers are killing Hollywood's home-video business. People are rapidly discovering new ways of watching films at home that pose a grave threat to the most profitable part of the film business.

In America, by far the biggest home-entertainment market, spending on videotapes and discs has dropped by 29% since 2004. Piracy is one reason. Another is the end of the format-replacement cycle: once you have a DVD of "Casablanca" you don't need another one-and you probably won't buy a high-definition Blu-ray disc, either. But the big reason is the rise of cheap, convenient rental outfits like Redbox, which runs kiosks, and Netflix, which streams some films and sends others through the post. The move from buying to renting is a calamity for Hollywood, a low-margin business that has come to rely on disc sales to push films into profitability.

Like music, newspapers and books before it, the film business has been disrupted by innovative, fast-moving distributors whose products have caught on with the public (see article). Tinseltown's attempts so far to see off the threat have fallen flat, partly because the studios have failed to co-ordinate their efforts. But if Hollywood moves quickly and boldly it should be able to disrupt the disrupters.

Led by Sony, a consortium of studios, technology firms and retailers are working on a new way of distributing digital copies of films. The idea is that consumers will be able to buy the rights to films stored "in the cloud" and stream them to any device. That should make buying more appealing. But it also gives the studios an opportunity to go straight to consumers.

At the moment Hollywood is a business-to-business industry: it rents films to cinema chains and ships discs to big-box retailers and rental firms. Digital distribution should allow it to become much more consumer-facing. The studios could greatly expand their efforts to sell films directly. They could offer to upgrade existing DVDs to digital files. At a minimum, they could develop customer databases that they could use to refine their marketing campaigns. The studios are old-school advertisers: every year they spend billions of dollars on scattershot campaigns that often hit the wrong people. Every dollar spent trying to persuade a grandmother to see a Quentin Tarantino film is a dollar wasted (Quentin's granny excepted).

Here's looking at you

Disney and Pixar are brands, but most studios are not. Nobody goes to see a film because it is made by Fox. Increasingly though the films they release are brands-consider "Harry Potter" or "Pirates of the Caribbean". The studios also employ actors and directors who are brands in their own right. They should market directly to people who love those brands.

It will not be easy to take such a radical step. But the trail has been blazed by another medium. Record labels have been hit much harder by piracy and have seen retail outlets disappear. They have been forced to deal directly with consumers. Lady Gaga's website is run not by the pop star but by Universal Music, which uses it, and the consumer information it collects, to sell directly to her fans. That outfit has become far better at mining consumer data than the film studios. A common refrain in Hollywood is that the film business must not go the way of music. In this sense, at least, it should.

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Letters

On farming and the future of food, high-speed rail in Britain, Egypt, China

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Letters are welcome via e-mail to letters@economist.com

Farming and food



SIR - Regarding the future of food (Special report, February 26th), there are two additional factors to existing and new technology that will raise farm output significantly. Large tractors and combines have transformed agriculture in the developed world, enabling far more land to be cultivated and crops to be harvested at speed, which reduces the loss caused by weather. Sixty years ago my father needed six men to grow 100 acres (40 hectares) of crops. Today my son can farm 1,000 acres with one man.

Agriculture in the developing world could also be transformed by this existing technology, but there needs to be fewer and bigger farms to make use of large equipment and to raise the collateral to invest. That means far fewer rural workers, and controversial social consequences.

New technology, such as satellite mapping, will enable farmers to identify wide variations of soil quality across every field and to adjust their equipment to apply their seeds, fertilisers and chemicals precisely at varying rates, depending on the fertility across the field. This makes great economic and environmental sense.

Chris Haskins
House of Lords
London

SIR - No solution to farming is viable unless we tackle the issue of consumption. In order to achieve a fairer balance in the world it would help if people in rich countries cut their meat and dairy consumption (which is also healthier). Crops should be used for feeding people, not for animal feed or biofuels. Research by the Potsdam Institute and the Alpen Adria University, in a study called "Eating the Planet", proposes feeding the world by 2050 using humane and sustainable farming without a big change in land use, but only if meat consumption is moderated.

Joyce D'Silva
Compassion in World Farming
Godalming, Surrey



SIR - Producing animal protein is costly in terms of land and water use. A cow needs up to ten kilograms of feed to produce one kilogram of meat. A pig needs around five kilos and a chicken around three. The best part of the world's maize and soyabean crops goes to feeding animals.

Separately, before poor farmers start buying seeds from big Western seed companies they should try some basic technologies such as crop rotation, green fertilisers and agroforestry. Those techniques, which are being implemented in many African countries, have the potential to increase yields and do much more to preserve the environment than planting large areas with one or two hybrid seeds.

Ernst Bertone Oehninger
Getulina, Brazil

SIR - Why not provide incentives for countries to curb excess consumption using phased-in tradable quotas? Countries failing to bring average consumption to below 3,000 calories a day could buy entitlements from grossly under-consuming countries, which could invest the proceeds in targeted grants aimed at eradicating the hunger that needlessly afflicts a billion people.

Andrew Macmillan
Scansano, Italy
Ignacio Trueba
Madrid



SIR - I was disappointed that your leader on food so readily dismissed the role of speculation in driving up food prices, alluding to Milton Friedman's old argument that "for every buy, there is a sell" ("Crisis prevention", February 26th). It is particularly surprising as *The Economist* has written repeatedly about the role of asset-price bubbles in exacerbating the financial crisis. Since Friedman's work more than 50 years ago, economists have developed strong theoretical foundations showing how rational asset-price bubbles can inflate for long periods of time; certainly long enough for a family to starve.

Moreover, there is considerable evidence that speculation in assets linked to commodity prices had an important role in driving up prices in the last food-price crisis in 2008. It is right, therefore, that the G20 should seek appropriate forms of regulation to discourage the formation of commodity-price bubbles, in addition to addressing the trade and agricultural policy issues you rightly mentioned.

Neil McCulloch
Institute of Development Studies
Brighton

SIR - In rich and poor countries alike, the principal underlying cause of wasted food is the lack of appropriate packaging. In poorer countries most wastage occurs from farm to shop; around half of all agricultural produce is spoiled before it reaches consumers. Foods spoil handled in bulk, without any protective packaging. Grains are infested by vermin, fruit and vegetables get bruised, meats are attacked by flies and maggots, eggs break and milk goes sour.

In rich countries, packaging and handling has vastly reduced this sort of waste. In those countries most of the waste is caused by consumers throwing away perfectly good food, in large part because grandma's taste-and-sniff test of food that is past its best-by date has fallen out of favour. High-tech packaging that changes colour to indicate the degree of rotting in food is becoming available. It reassures consumers and helps them reduce wastage.

In rich and poor countries alike, ensuring that adequate packaging is available will go a long way to feeding the world.

Julian Carroll
European Organisation for Packaging and the Environment
Brussels



SIR - You were wrong to claim that traditional and organic farming methods cannot feed the world. Scientific evidence has implicated intensive farming in the rise of two serious superbugs: a new strain of methicillin-resistant *Staphylococcus aureus* (MRSA) in farm animals, which is spreading rapidly and transferring to humans; and a new and almost untreatable type of *E.coli* that is causing a large number of deaths in Britain and elsewhere.

Evidence is mounting too of the problems that GM crops are causing for farmers. Weeds resistance to glyphosate have become a big problem in GM herbicide-tolerant crops in North and South America, while the cost of GM seeds cuts into farmers' incomes.

Georgia Catt
Soil Association
Bristol

SIR - GM crops are the answer for many African farmers. It is the cruel propaganda of European activists, sadly swallowed by the ruling African urban class, that prevents poor farmers from access to this lifeline. GM seeds are offered free to African farmers by Monsanto. And yet, out of fear or a neocolonial mindset, farmers refuse to take up the offer, lest they offend their European masters.

I see my neighbours, small landholders, desperately trying to extend their acreage and continually being pushed back to their one hectare. They see weeds smothering their maize and forcing them to abandon the rest of their field to return to the part that they already weeded but where more weeds are coming up.

Father Athanas Meixner
Soni, Tanzania

SIR - I have decided to take your special report on feeding the world and use it to make a compost heap to grow some wonderful organic vegetables in protest at your outright dismissal of organic farming and blatant proselytising on behalf of Monsanto.

Jonathan Shintaku
Los Angeles

Very fast rail



* SIR - You questioned whether our proposed scheme "High Speed Two", a 225mph railway line from London to Manchester and Leeds by way of Birmingham, "is a good idea" ("The need for speed", March 5th). HS2 would transform our economic geography, bring our big cities closer together, enable businesses to operate more productively and support job creation, growth and regeneration.

Our demand growth forecasts, which you question, are quite conservative. Demand for long-distance rail travel more than doubled between 1994 and 2009, an annual growth rate of around 5%. We have forecast a far slower growth rate of under 2%.

There is clear evidence that passengers value savings to the time. However, factoring this in would have no significant overall effect on HS2's business case as it would capture all the positive benefits experienced by travellers who switch from cars and planes, where it is impossible, or at least much harder to work, to high-speed rail, as well as the additional productive time made possible by reductions in overcrowding that HS2 will bring.

You were also right that HS2 will never produce the cost-benefit ratio of a road junction improvement or a new roundabout, but if the government concentrated all its money on just the schemes with the highest cost-benefit ratios, but ignored wider benefits, Britain would have fantastic roundabouts, but no Jubilee line extension, no Channel Tunnel and no Crossrail.

Our competitors are pressing ahead with ambitious high-speed rail plans. We cannot allow Britain to be left behind.

Philip Hammond, MP
Secretary of state for transport
London

Egypt's economic woes

* SIR - Egypt is indeed still "mired in troubles", but these are not just political ("It's not over yet", March 5th). The jobless rate is as high as 40% among the youth. Around 44% of the population subsists on less than $2 a day. Over the past decade the Egyptian pound has lost almost half its value against the dollar. Costa Rica exports more than Egypt.

More than 90% of Egyptians hold their property without legal title. The value of this property is estimated to be 30 times greater than the market value of registered companies. Some reports suggest that to open a small bakery requires more than 500 days, through 56 government agencies and repetitive government inspections. To get legal title to a vacant piece of land requires more than ten years of dealing with red tape.



About 35% of the working population, or 7m people, are employed by the public sector. Civil servants are hired, assigned, supervised and promoted haphazardly, usually in offices without proper equipment or facilities. Most are so poorly paid that they are extremely impoverished unless they hold additional jobs and rely upon various forms of corruption.

Some 20% of Egyptians own nearly 80% of the country's wealth. Their children go to private schools and subsidised universities. Much of the wealth of the upper-income group is derived from undocumented sources, making a progressive income-tax system extremely difficult.

Until government and the legal system improve in Egypt, and tax is collected properly, ordinary Egyptians will remain frustrated by the lack of socioeconomic progress. Although we should be happy at the overthrow of Hosni Mubarak, we should also remember the French saying: The more things change, the more they remain the same.

Herbert Werlin
College Park, Maryland

Stamping on the petals of democracy

* SIR - It is a sad state of affairs when the Chinese government is worried about a little folk song inciting revolution. I wonder if Puccini's Turandot would now be banned in China, since the composer made liberal use of "Beautiful Jasmine Flower" in his opera? ("No awakening, but crush it anyway", March 5th).

Patrick May
Vancouver

* Letter appears online only

Japan's catastrophes

Nature strikes back

Can fragile Japan endure this hydra-headed disaster?

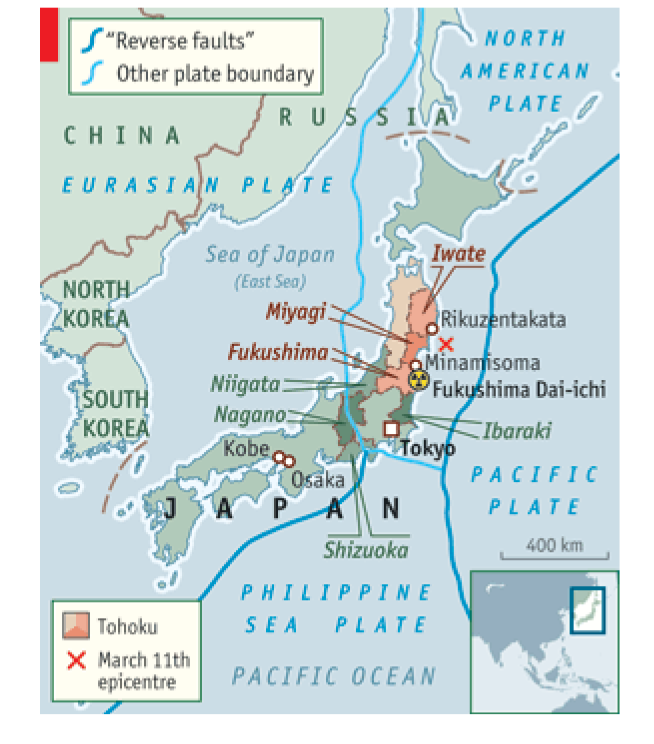


UP A shallow river, five kilometres from the Pacific coast in Japan's north-eastern Iwate prefecture, lie the remains of a town. Crushed wooden houses now resemble matchwood, scattered in every direction over swampy wasteland. A purple car is partially submerged in mud. The piles of debris reach two metres high.

Only on close inspection do you see that it was never a town at all-at least not there. It was a rice paddy. The houses, shops, cars and people belonged lower down the valley. But the town is gone, washed away. Its debris settled on the field, high up the valley, that was the tsunami's high-water mark. That is all that physically remains of Rikuzentakata.

Rikuzentakata, a former whaling town, once held 23,000 people. Several hundred are confirmed dead, but at mid-week perhaps thousands more were still missing. All tried to flee, as they were trained to do, when the tsunami warnings sounded in mid-afternoon. But this was a town of old people, as fishing villages here invariably are. Many just could not make it. Their fate was shared by perhaps tens of thousands of people living in ports, coastal towns and tiny cove communities across the north-east. Some, though, were spared. Above a washed-away hamlet clay-tiled homes are still standing, and a garden with tenderly coiffed trees. Even higher up is a small cemetery.

Japan, which shows its love of nature in its reverence for trees and seasons, also knows the awesome power of the physical world-and fears it. Its orderly and law-abiding people know they live on one of the most geologically violent archipelagoes on the planet. The earthquake that struck on the afternoon of March 11th had a magnitude of 9.0, the biggest in Japan's recorded history. It was so strong that, even in Tokyo's shock-absorbing skyscrapers, office workers cowered beneath their desks and then raced out into the street, only to be hit again by the whump of aftershocks.



As the quake lifted the ocean floor, it triggered a tsunami (the word is Japanese) that breached with ease some of what were considered to be Japan's best coastal defences. As of March 17th the police said at least 14,000 people were dead or missing along the coast, though that fails to account for the tens of thousands who are unreported to the authorities, supposed lost, in places like Rikuzentakata. As many as half a million are in emergency shelters, shivering through a bitterly cold snowstorm that has added to the sense of crisis. Because of damaged roads, petrol shortages and bungling bureaucrats, many lack essentials such as food, water, toilet paper, nappies and kerosene for heating. A shocking number appear to be in their 90s, looked after by people who are themselves grandmothers and grandfathers. Amid the debris in Rikuzentakata, a 62-year-old woman wearing trainers was prodding around for her 94-year-old aunt. The president of a nearby construction company had tried to help the aunt escape, but he too was washed away. Her niece had been searching fruitlessly for her every day since March 12th.

Appalling as these people's plights are, they have been eclipsed for most of the week by fear of an altogether different sort: that of a meltdown in the damaged Fukushima Dai-ichi nuclear-power plant, some 240km north-east of Tokyo (see article). Nuclear experts say the potential danger to human health from the three stricken reactors has so far been blown out of proportion-especially when set against the wider-spread suffering of the tsunami victims. But there is a gnawing sense that Japan, the only country to have suffered mass radiation from atomic attack (and hence an expert in its consequences for long-term health), may be on the verge of another nuclear nightmare. Inevitably, the latest crisis will renew debate about the wisdom of building nuclear-power plants on such unstable and exposed terrain. Experts, however, can barely imagine Japan meeting its energy needs without them.

A government under siege

The palpable fear of the unknown can be heard in the words of Katsunobu Sakurai, the mayor of Minamisoma. His town straddles the 20km exclusion zone surrounding the Fukushima plant, as well as the 30km circle in which as many as 136,000 people are being urged to stay indoors to avoid radiation. Speaking by telephone to NHK, Japan's national broadcaster, on March 16th, he said that people were now "trying their best to stay calm", but many would flee the area altogether if they could only find fuel to make the journey. He said the most basic supplies were running short because outsiders were not willing to transport them to the danger zone. Whenever he is interviewed, he begs the government for help.

The government, though, is besieged on many fronts. Naoto Kan, the prime minister, entered a crisis of hydra-headed complexity with feeble popularity and little public respect. Until Mr Kan's Democratic Party of Japan took power in 2009, Japan had seen its institutions of government corroded by 55 years of one-party rule; and one of the biggest bones of contention had been the nuclear-power industry.



Reduced to this

Generally the safety record has been good, considering the number of plants and their length of service. But when there have been accidents, a shameful record of cover-ups, lackadaisical crisis management and an inbred complicity between regulators and utilities has given the public ample reason for scepticism.

The first response of Mr Kan, a former civil activist, has suggested that he is reacting more openly, though he hardly exudes authority. If his presence has been hit-and-miss during the crisis, that cannot be said of his steadfast chief of staff, Yukio Edano. Mr Edano has produced frequent updates on the unfolding nuclear crisis, while avoiding sowing panic among the public. In his blue overalls (now standard kit for Mr Kan and his team), he looks to many the epitome of the stalwart line manager.

But if the Fukushima crisis worsens, Mr Kan's ability to lay blame for the mishaps on the Tokyo Electric Power Company (TEPCO), the owner of the power plant, will wear thin-not least because the government has set up a crisis committee with TEPCO that appears to put the company firmly in charge. Also, there is the lingering danger of panic. Foreigners with families in Tokyo have reacted most nervously. As the radiation has risen they have taken bullet trains to Osaka, in western Japan, and flights out of the country, quietly supported by their firms and embassies.

Most residents of greater Tokyo-at 35m, the most populous metropolitan area in the world-have shown much more stoicism, partly because the authorities and media have remained calm. Despite radiation fears, aftershock warnings, power cuts, train disruption and half-empty supermarkets, many queued patiently on March 15th to meet their tax deadlines. But the next day, reflecting the seriousness of the situation, 77-year-old Emperor Akihito gave a rare televised address to express his "deep concern". He had been quiet until then, despite messages of support coming in from royalty around the world.

For the authorities, one increasingly apparent danger is that the nuclear drama is distracting them from what should be an equally pressing priority. They need to find a way to move supplies to the stricken towns and villages in the north-east. Takeshi Niinami, chief executive of Lawson, Japan's second-largest chain of convenience stores (which lost 68 stores in Friday's disasters, with more than 100 staff unaccounted for), says that the urgent priority is to renew fuel supplies to Tohoku, the north-eastern region and the scene of the disaster. Without fuel, he says, local factories have been unable to produce rice balls and other food supplies; nor is there enough petrol for food brought from elsewhere in Japan to be trucked to the hardest-hit areas.

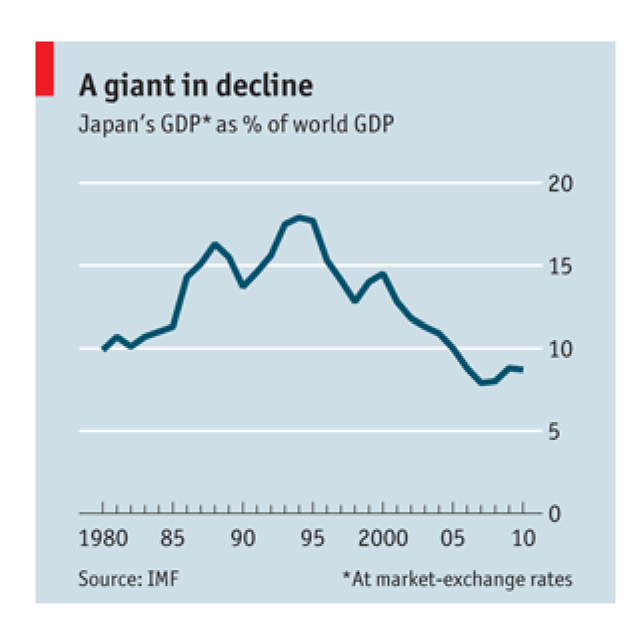
Mr Kan has ordered 100,000 troops from Japan's Self-Defence Forces to the region, but according to Mr Niinami their task is to find dead bodies rather than distribute supplies. He has urged the authorities to divert passenger planes to help airlift provisions. Others in the affected region blame the bureaucratic mindset of civil servants for blocking the flow of emergency supplies.

Layered over the humanitarian and nuclear drama is yet another mounting concern: the effect on Japan's economy. It is in a parlous state, suffering from slow growth, high debt and relative decline (see chart). Many economists at first suggested that things were not as bad as they looked. Of course, there would be a short-term dip in growth. But as reconstruction began, growth would pick up again. The international impact, too, would be limited. Supply-chain disruption would cause some problems, especially in the electronics industry, but overall the expected boost in Japanese imports as it rebuilt would help the rest of the world.

That, at least, is what the history of recent Asian disasters suggests. The tsunami of December 2004 and the Kashmir earthquake of October 2005 involved death and destruction on an even wider scale, yet had virtually no impact on growth rates. That was largely because the victims were mostly poor people who added little to GDP. But even the Kobe earthquake of 1995-the second-biggest ever to hit a modern urban area-had a surprisingly modest effect (see article). Within 15 months industrial production in Kobe had almost reached pre-quake levels, and Japan as a whole suffered only one quarter of declining output.

A second reason to expect the economy to cope is that although the area affected by the tsunami and quake was vast, it contains no Kobes. It is less populated and less industrialised. According to calculations by economists at Nomura, an investment bank, the three worst-hit prefectures (Miyagi, Fukushima and Iwate) account for just 3.6% of Japan's economy, though electronics factories are clustered there.

Adding in neighbouring Nagano, Ibaraki and Niigata prefectures, which were much less damaged, brings the affected area's contribution to GDP to 10.8%. That is a big chunk. But Tomo Kinoshita of Nomura nevertheless estimates that the direct negative hit to Japan's GDP would be limited to between 0.25 and 0.5 percentage points in the first quarter, and 0.5 and 1 percentage point in the second. Another bank, Goldman Sachs, estimates the cost of the damage at Â¥16 trillion ($202 billion), or about 4% of GDP. Spread over a few years of reconstruction, that should easily be affordable-a drop in the ocean of Japanese public indebtedness.



However, first guesses about the disaster's impact have been overtaken by further disasters. The nuclear crisis at Fukushima broadens the economic danger in at least three ways. First, the perceived risk of radiation may close businesses, deter investment and hamper rebuilding. TEPCO, with its shares hammered, now faces worries about its creditworthiness. And selling nuclear-energy technology abroad-Toshiba, Hitachi and Mitsubishi Heavy Industries all produce reactors-is one of the linchpins of Mr Kan's growth strategy.

Second, electricity rationing may keep output depressed for longer than originally anticipated. Only a week after the quake, Tokyo was facing rolling blackouts. And third, the nervous mood makes financial panic more likely. Over three days the Bank of Japan announced plans to inject a total of Â¥55.6 trillion into financial markets, to avoid a collapse in investor confidence and keep credit flowing. On March 14th and 15th shares on the Tokyo exchange fell by over 16%, their worst two-day fall since 1987. They have recovered somewhat since, but the yen also strengthened to record highs against the dollar. A nuclear meltdown may yet lead to a financial one. That would add another international risk-financial contagion-to all the other dangers looming over Japan.

Supply-chain concerns are mounting as it becomes apparent that more Japanese factories may be closed for longer than first thought, and that a surprising number of gizmos assembled in China, South Korea, Taiwan and elsewhere depend on

Japanese components. There were also fears that the price of oil, which at first fell a bit because of an expected drop in Japanese demand, might be driven even higher as Japan makes up for the shortfall in nuclear power, at a time of tensions in north Africa and the Middle East.

Phoenix in the east

The tasks facing Japan are staggering. But a country does not live on a geological time bomb without some accommodation by the national psyche. The legacy of centuries of rebuilding cities, temples and homes after tsunamis, fires and earthquakes has provided many Japanese with a fatalistic streak. In the past they have often risen to the task of rebuilding; it provides a sense of national purpose.

Twice in the past century, Tokyo has re-emerged out of the rubble. After the Great Kanto Earthquake of 1923, in which 143,000 people died, the recovery turned poisonous; amid the wreckage, sword-wielding Japanese set about wantonly killing Korean immigrants. Democratic shoots were trampled, and nationalistic passions eventually drove Japan to war. Two decades later, in 1945, destruction came from American bombs. The zeal to rebuild was again remarkable. Within a generation, Japan had turned-peacefully this time-from one of the chief recipients of World Bank aid into an industrial superpower.

The past 20 years of stagnation and deflation-albeit with high levels of conspicuous consumption-have left many yearning for a new sense of purpose. It is perhaps a chilling reflection of this that comments by Shintaro Ishihara, the right-wing governor of Tokyo, harking back to imperial days by calling the disaster "divine retribution" for Japan's culture of "greed", have found some resonance, especially among elderly Japanese. Others will be furious.

More thoughtful voices propose more constructive ways to forge a new sense of purpose. Many foreigners have expressed deep admiration for the calm resilience the Japanese have demonstrated this week (see article). A university professor, stuck for 25 hours on a short train journey to Tokyo as a result of the earthquake, wrote a long piece on Facebook about the patience of his fellow passengers, the solicitousness of the railway staff, and the spotless toilets. "If you have to spend 16 hours in a stationary train and an additional nine hours getting home, do it in Japan," he wrote. Japanese people say they take heart from such commendations.

As for the future, Hideaki Shiroyama, a public-policy expert at the University of Tokyo, says a big indication of Japan's willingness to shake off its lethargy will be the inevitable debate on nuclear energy that emerges from the disaster. Part of the public scepticism about the industry, he believes, stems from a regulatory structure that remains mired in the past. The industry is fiercely tribal, and regulators are too close to the utilities. Even before the emergency, he says, calls from within the industry for change went unheard.

Similarly, he says Japan's policy towards rebuilding fishing communities such as Rikuzentakata will be a chance to think creatively. An enlightened response would be for many of the demolished communities to be abandoned for ever, because in Japan's greying society their residents are mainly pensioners. It would make more sense to rehouse them in higher-density communities closer to shops and hospitals. But even those whose houses have been destroyed by the tsunami are loth to leave-these are ancestral plots that are meant to stay in the family. And the fishing grounds are rich. Since Japan instinctively solves any economic problem by throwing concrete and dollops of public money at it (tight as money is), the elderly will probably get their way.

The rebuilding, as well as the discussion about Japan's future energy sources, might be easier if the political system encouraged debate and compromise, rather than partisan gridlock. To rebuild Japan, the public spirit shown by citizens in the face of today's catastrophe needs to inspire the political class, promoting collaboration and unity. As Mr Kan says, Japan has to pull together. If the earthquake helps Japan repair its social fabric and recover its sense of purpose, it may yet bring something other than tragedy in its wake.

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Plate tectonics

Faulty thinking

The myth and reality of the Japanese earthquake



BACK in January, Japanese seismologists warned that the tectonic plates colliding beneath the Pacific Ocean off the north-east coast of Japan were poised to slip catastrophically. By their reckoning, there was a 99% chance of an earthquake of magnitude 8.0 occurring off the Miyagi coast, and a 90% chance of one off Ibaraki prefecture, within the next 30 years. They were surprised only by the sheer size of the magnitude 9.0 monster that was unleashed when the plates at last let go on March 11th.

It seems that, on occasions, the rupture along this particular type of "reverse fault" (where the upper part of one side of the fault is thrust over the foot of the other) can jump across gaps and other boundaries along the fissure, linking up with other parts of the fault to extend the breach alarmingly. The traditional fault-segmentation model used in seismology does not allow for this. But on that fateful Friday, when the North American plate slid over the Pacific plate along a subduction zone running 130km (80 miles) off the Pacific coast of northern Japan, the shock leapt from the first segment to a second and on to a third, extending the fault zone some 400km and increasing its intensity more than 30-fold. With all the action taking place only 24km down, the seabed was thrust violently upwards, triggering huge waves.

Could such a chain of seismic events happen elsewhere in Japan? Many in Tokyo fear that earthquakes may be creeping closer. The Japanese media have drawn attention to a quake of magnitude 6.6 on the far side of the country, between Nagano and Niigata prefectures, and to a quake of magnitude 6.1 in Shizuoka prefecture, both within days of the main quake. But these fairly common events occurred on entirely different tectonic plates. It is hard to imagine how faults on one continental plate might communicate with those on another that is hundreds of kilometres away.

No doubt Tokyo will be sideswiped one day. The most likely spawning ground for that earthquake will be 100km or more to the south-west, where the Philippine plate dives under the Eurasian plate, creating a continuous sequence of shudders. This could feasibly cause a megaquake of the kind the north-east has just suffered. But the evidence remains largely against it.

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Japan's nuclear industry

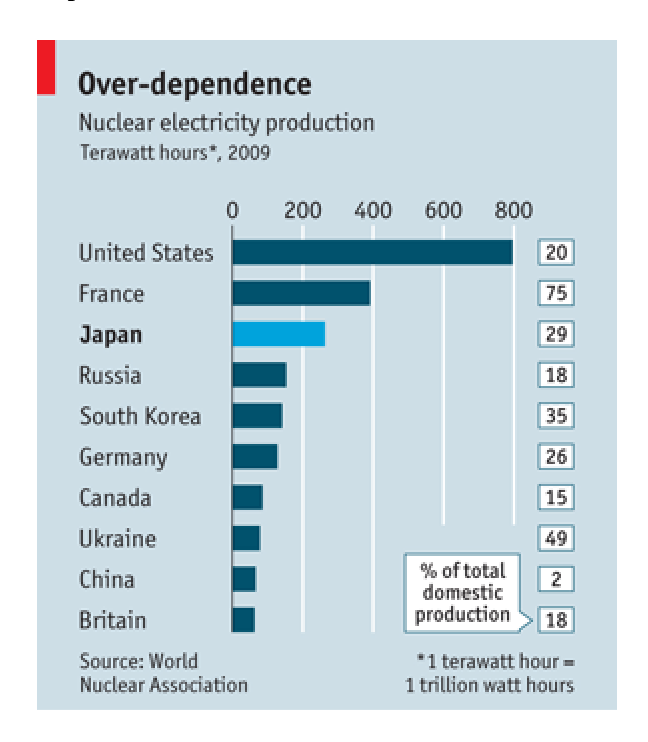
The risks exposed

What the damage to the Fukushima plant portends for Japan-and the world



Reliving the horror their grandparents knew

ONE danger of earthquakes, from Tokyo to San Francisco, has always been the flames that rise from the wreckage when fires are unleashed from their hearths. In Japan they have been called the "flowers of Edo". But no earlier flames have been as foreboding as those that have erupted sporadically from the stricken Fukushima Dai-ichi nuclear power station. The horrifying spectacle will not end the planet's nuclear endeavours. It could, however, reshape them radically.



Of the nuclear plants that provide about a third of Japan's electricity (see chart), Fukushima Dai-ichi is not the first to be paralysed by an earthquake. But it is the first to be laid low by the technology's dependence on a ready supply of water for cooling. To be near water is usually to be near the sea. And in this case, that meant right in the path of a tsunami.

The immediate impact of the catastrophic failures at Fukushima is not yet clear. It is worse than America's near-disaster at Three Mile Island in 1979, which was fairly swiftly brought under control. But it is highly unlikely to be as devastating as the accident at Chernobyl in Ukraine in 1986, which sent a radioactive cloud across Europe that caused the deaths of an uncertain number of people, possibly well into the thousands.

The 40-year-old reactors in the nuclear power station run by the Tokyo Electric Power Company faced a disaster beyond anything their designers were required to imagine, and shut themselves down appropriately. They might have got through

comparatively unscathed, as did the reactors at Fukushima Dai-ni, a similar plant farther along the coast. But at the Fukushima Dai-ichi plant things went wrong in many ways.

Nuclear reactors are protected by what plant designers call "defence in depth". Some of these defences are simple barriers. The nuclear fuel is encased in hard alloys to construct fuel rods; the reactor core that these rods make up, and the water it sits in, are contained within a steel pressure vessel. That in turn sits within a larger steel structure, the primary containment vessel. Around it sits the steel and concrete secondary containment structure.

Other defences are actions, rather than things. The first action to be taken in the case of an earthquake is an emergency shutdown, which is achieved by thrusting control rods that sit below the reactor in its pressure vessel up into the reactor's core. The control rods soak up the neutrons that mediate the chain reaction which produces most of a reactor's energy, shutting it down. But other reactions will continue for a while; straight after shutdown, a reactor like those at Fukushima Dai-ichi is still a heat engine as powerful as a fair-sized jet engine at full throttle, locked in a small tight box. Things can get hot pretty quickly if there is no way of keeping it cool.



And after the tsunami hit, Fukushima Dai-ichi lost its cool. Generators stopped; electrical switching equipment was flooded. Attempts failed to get the cooling system working with batteries and generators from elsewhere. The emergency power eventually ran out altogether.

The Fukushima Dai-ichi plant uses boiling-water reactors, which are basically electric kettles where the nuclear reactor is the heating element at the bottom. If the kettle can't be turned off and its spout is bunged up because the steam is radioactive, the situation inside will deteriorate. The amount of water will decrease, until eventually the nuclear core at the bottom is uncovered. It then gets even hotter even quicker, and bits of it will start to melt and react with the steam. The steam, meanwhile, will become ever more plentiful, and pressure will build up to a potentially explosive level. This seems to have happened to some extent in all three reactors.

In reactor 1, and later in reactor 3, steam contaminated with some radioactive elements was allowed out of the pressure vessel and into the larger containment vessel that surrounds it. There hydrogen in the released gas met a spark and exploded, blowing the roofs off the buildings but not, it seemed at the time, damaging the containment systems. With the primary containment vessel of reactor 1 still too full of steam, the radical decision was made to flood it with sea water to absorb the heat. The sea water was also laced with boric acid, which can soak up stray neutrons that the control rods miss.



Fukushima Dai-ichi: trying to explain

Reactor 3's pressure vessel was then treated the same way, as, eventually, was reactor 2's. But at some point, according to the company's reports, reactor 2 boiled dry, and also-the two things possibly connected-suffered damage to the doughnut at the bottom of the containment vessel in an explosion on Tuesday morning. That is why it was reactor 2 which, by March 15th, was posing the greatest threat. Later it was reported that the containment was compromised at reactor 3 as well.

At around this stage the problems of the deteriorating plant began to spread. On March 15th, and again on the 16th, fires started in the building housing reactor 4. The reactor was safely off-line for maintenance when the quake struck, but there is spent fuel in storage tanks in the building, as elsewhere in the plant. This, too, needs to be covered with water that is circulated so as to keep things cool. At reactor 4 and reactor 3 spent fuel may have been exposed to the air. After the fire, radiation levels inside the plant soared. At this point, the level outside the plant was fairly high too. At one stage an unprotected person at the main gate would have received the maximum allowable yearly dose for a nuclear-industry worker in a matter of hours.

Conflicting reports of how much radiation was spreading farther afield were enough to cause panic. Matters worsened when America announced that it thought radiation levels were extremely high, and could severely constrain efforts to control the situation. On March 17th these included the use of helicopters and possibly water cannon to top up the water in the spent-fuel stores, bulldozing new access paths and yet more efforts to supply the plant with reliable electricity from the grid.

Chain reaction

The Japanese are now sure to reconsider their reliance on nuclear power, which is currently provided by 55 reactors, many similar in design to those now in trouble. Despite high spending on solar power over the years, the only real alternatives are imported natural gas or dirty coal. In the short term, with large parts of the country's nuclear-generating capacity shut down, more gas will have to be imported. If the long term has a lot less nuclear power in it, there will be a corresponding need for gas and probably coal.

What of the rest of the world? Industry boosters had hopes of a nuclear renaissance as countries try to cut back on carbon emissions. There has been talk of a boom like that of the 1970s, when 25 or so plants started construction each year in rich countries. Not any more. Public opinion will surely take a dive. At the least, it will be difficult to find the political will or the money to modernise the West's ageing reactors, though without modernisation they will not get any safer. The searing images from Fukushima, and the sense of floundering haplessness, will not be forgotten even if final figures reveal little damage to health.

The German government has declared a three-month moratorium on its controversial plan, agreed only last autumn, to prolong the life of its nuclear plants. This is likely to lead to the shutdown of its seven oldest plants and their permanent

removal from the power grid. America's never more than limited enthusiasm for new nuclear plants may disappear altogether.

If there was nothing else the matter, the nuclear industry might be able to weather a not-too-bad final outcome at Fukushima. After all, new reactors are said, with some justification, to be a lot safer. And most countries have the option of building them in seismically inactive zones, a luxury Japan does not enjoy. Even old reactors in the West, such as America's boiling-water reactors, have been revamped in such a way as to preclude, it is thought, anything like the power outage that doomed the similar reactors at Fukushima Dai-ichi. But something else is the matter. Although the new reactors may be much safer than the old ones, they are a lot more expensive.

It is hard to say how much more expensive, since so few are being built. Generous loan guarantees have failed to get any commissioned so far in America. Two are under construction in western Europe, and both are over-budget. The labour of getting safety approvals makes investors jittery. And natural gas is abundant, far cheaper and relatively clean.

Yet the world will not necessarily turn en masse against nuclear power. Although events at Three Mile Island halted construction of nuclear plants in America, elsewhere-in France and, strikingly, in Japan-it continued. France, which has 58 nuclear reactors, seems to see the disaster in Japan as an opportunity rather than a setback for its nuclear industry. President Nicolas Sarkozy sang the industry's praises on March 14th, saying that French-built reactors have lost international tenders because they are expensive: "but they are more expensive because they are safer."

But the region where nuclear power is set to grow fastest, and seems least likely to be deterred, is the rest of Asia. Of the 62 plants under construction in the world, two-thirds are in Asia. Russia plans another ten. By far the most important nascent nuclear power is China, which has 13 working reactors and 27 more on the way. China has announced a pause in nuclear commissioning, and a review. But its leaders know that they must move away from coal: the damage to health from a year of Chinese coal-burning dwarfs any caused by the nuclear industry. And if anyone can build cheap, one-size-fits-all nuclear plants, it is probably the Chinese.

If the West turns its back on nuclear power and China ploughs on, the results could be unfortunate. Nuclear plants need trustworthy and transparent regulation, a clear distinction between operators and regulators and well enforced building codes. The Fukushima plant lacked some of those. China can offer none.

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Health care

A not very happy birthday

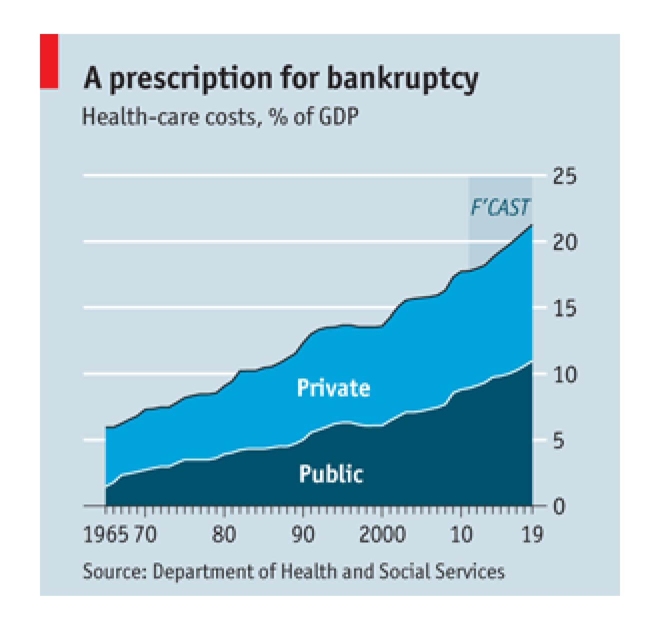
What will become of Barack Obama's health reforms?



WHEN Barack Obama signed a sweeping set of health reforms into law on March 23rd 2010, he knew it was a historic moment-and not just because Joe Biden, the vice-president, whispered into his ear that it was a "big fucking deal". He had successfully ridden the wave of popular support that brought him into office to deliver universal health coverage, a feat that eluded all his predecessors.

But the reality of politics has obstructed that grand dream. Republican leaders in Congress are trying to repeal the law outright. Several federal judges have ruled that one of the central provisions of the new reforms, an "individual mandate" requiring everyone to purchase coverage, is unconstitutional. And a recent poll by the Kaiser Family Foundation (KFF), a non-partisan outfit, revealed that hostility to the laws among politically vital independents has shot up sharply. One year on, how fares Mr Obama's proudest achievement?

The chief strategy used by the administration to win over sceptics and to undermine legal challenges is to present the new laws as an unstoppable juggernaut. For example, when Kathleen Sebelius, the secretary of health and human services, spoke about the reform to the Senate Finance Committee on March 16th, she pointed to evidence of an "enormous difference it has made in the lives of Americans".



True, the administration has rushed into force provisions affecting consumers directly, in an effort to win popular support. For example, some forbid insurers from denying coverage to children with pre-existing conditions, or imposing lifetime payout caps on anyone. The new laws also already require insurers to cover children up to 26 on their parents' policies, which will benefit some 1.2m young people. Nearly 48m people on Medicare, the government health scheme for the elderly, are to get free preventive services such as colonoscopies and mammograms. In 2010 nearly 4m of them got $250 tax-free rebates to help pay for drugs.

All that seems impressive, but here's the rub: many Americans do not believe Mrs Sebelius. Roughly half of those polled by KFF thought Obamacare had already been repealed or were unsure of its legal footing. It remains the law of the land.

The administration is also forging ahead with less visible aspects of the new laws. By 2014, when the bulk of the reform's provisions kick in, states are required to have put regulated insurance exchanges in place so that consumers can buy plans that meet minimum standards for coverage. All would be required to buy insurance, but the less well-off will get subsidies. The federal government is offering technical assistance as well as money to states to nudge them towards establishing such market-places.

Alas, in this too Mr Obama has hit snags. Some Republican-led states, first among them Alaska and Florida, are refusing to take the money, while many others are demanding flexibility in implementing the rules. To the surprise of some, Mr Obama announced at a recent meeting of governors at the White House that he supports a plan-first proposed by Ron Wyden, a sparky Democratic senator-to grant "innovation waivers" starting in 2014. As long as states meet general goals on covering more people and curbing costs, they will be given flexibility in how they set up their local insurance markets.

That compromise comes only at the point of a gun, however. And Republican attacks on Obamacare will increase as next year's presidential race gets under way. That points to a second question: can such attacks actually kill the reform? It seems unlikely. While Mr Obama is president, he would veto any such bill. So the legislative path to "repeal and replace", as conservatives call it, hinges on winning back both the Senate and the White House. But that is far from a certainty, and the short-term strategy of defunding bits of the scheme looks more likely to score points than actually stop the law.

The other great hope for enemies of reform is that the Supreme Court will declare that the individual mandate is unconstitutional, and that this will lead directly to the unravelling of the dread laws. This too may prove unsatisfying for conservatives. For one thing, the court may not immediately take up this matter, giving boosters of the laws the chance to dig in their heels. For another, the individual mandate can be replaced with other policies-a mix of carrots and sticks to get punters to buy insurance-that imitate it. So such a ruling would be a political nightmare, but need not be a death blow to reform itself.

Given all this, what will be the likely long-term impact of Obamacare? Critics say that if the law stays in place, it will destroy employer-provided health coverage. Boosters insist that if it is given a chance to work, it will bring costs down, and not merely extend coverage. Both camps are probably wrong.

Republicans have often claimed that employers will scrap corporate insurance, preferring to pay a fine and dump their workers on the subsidised exchanges. That sounds plausible, but two new studies-by the RAND Corporation and the Urban Institute, both non-partisan think-tanks-debunk the argument. In fact, the boffins at RAND calculate that the new reforms could even increase employer-sponsored coverage, as employees confronted with the new mandate clamour for (tax-assisted) coverage from their employers now that they are obliged to have it.

As for costs, Mr Obama's reforms deserve praise for expanding coverage, but they do this by adding millions of people to an unsupportably expensive system. Analysts estimate that America's health spending will continue to soar under the reforms (see chart). That is a point hotly contested by Mr Obama's team, who usually point to theoretical future efficiency gains and innovations that will save pots of money.

So it came as a shock when Deval Patrick, the governor of Massachusetts and one of Mr Obama's closest friends, took a different tack. Asked recently about the pioneering health reforms in his state, which served as a model for the national reforms, he first gave a backhanded compliment to Mitt Romney (the state's former Republican governor, now distancing himself from those reforms as he repackages himself to run for president in 2012). Mr Patrick then revealed the dirty little secret of Obamacare: "What these folks did in Massachusetts is frankly the same thing that the Congress did, which is to take on access first, and come to cost-control next." In other words, America will soon have no choice but to come to grips with costs. Whatever one thinks of Mr Obama's reforms, there is no denying that they have brought that day of reckoning closer.

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The budget

The sixth fudge

Yet another short-term fix looks likely



"THIS is a lousy way to run a railroad," complained Steny Hoyer, a senior Democrat in the House of Representatives. But at least the trains are still running. On March 15th the House approved a stopgap measure to keep the federal government running until early April. As *The Economist* went to press, the Senate looked set to do the same. For three more weeks, it seems, a shutdown of all but the most essential bits of the government has been averted. But a derailment still looms thereafter.

For almost six months now, the government has been subsisting on a series of short-term "continuing resolutions" in lieu of an annual budget. That has allowed congressional leaders to skirt divisions about how much the government should be spending. But the divisions remain.

The latest continuing resolution follows the same formula as the previous one, passed two weeks ago. It cuts annual spending by $2 billion for every week of the government's reprieve, for a total of $6 billion in this case. That allows Republicans, who want to take an axe to the budget, to claim they are chopping away. But all the items cut so far are things the Democrats had already agreed to do without, either through Barack Obama's proposed budget for next year or through a ban on earmarks, meaning individual congressmen's pet projects.

The drawback of this approach is that the two sides are running out of cuts they can agree on. Republicans are eager to scrap all spending on cherished Democratic causes, such as Mr Obama's health reforms and public broadcasting. That, naturally, is anathema to many Democrats, who anyway feel that the cutting has already gone far enough. Besides the $10 billion trimmed from the two most recent continuing resolutions, they point out, spending was already running at around $40 billion below the level Mr Obama had proposed for the year in his never-enacted budget. Given that the Republicans had set a target of cutting $100 billion, says Jay Carney, Mr Obama's spokesman, the Democrats have already met them halfway. Many Republicans, however, think $100 billion too timid and their leadership's reluctance to use the threat of a shutdown to extract bigger concessions from the Democrats too craven.

Support for a compromise, or at least for the fudge embodied by the continuing resolutions, is dwindling. Whereas only six Republican representatives voted against the previous continuing resolution, 54 of them rejected the latest one. That meant that the Republican leadership in the House needed 29 Democratic votes to secure its passage. Yet Democratic support also fell, from 104 votes in favour last time to only 85 this time.

The Senate, meanwhile, seems hopelessly divided. Neither the Democrats' modest cuts, nor the Republicans' savage ones, won the support of a majority in recent votes, let alone the 60% threshold of support needed to pass most legislation. In short, the two parties remain on a collision course, with the train wreck currently scheduled for April 8th. By then, the

government will be about to bump up against the federal debt ceiling, any increase in which requires congressional approval.

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Education policy

Final exam

As elections loom, Barack Obama tries to reform America's schools

AMERICA'S schools are dotted with stories of progress. In December your correspondent watched a class of seven-year-olds on Chicago's poor West Side. As Mauricia Dantes, a consultant for IBM before she retrained as a teacher, led the pupils in a discussion about the deaf-and-blind author Helen Keller, one small girl declared: "I feel like I'm in college." One day, thanks to Ms Dantes and other teachers, she may be.

Barack Obama wants such scenes to be the rule rather than the exception. The question is what the federal government can do to help. Ten years ago Congress passed the No Child Left Behind Act (NCLB), a bold effort to improve America's schools. On March 14th Mr Obama announced that he wants to pass a new version by August. It could be one of his most important feats. But it will not be easy.

The main problem is that politicians still disagree on Washington's role in education. The federal government provides less than 10% of the money schools spend. But NCLB, the most recent incarnation of the 1965 Elementary and Secondary Education Act, gave the federal government unprecedented influence. States must set standards of achievement. Schools that fail to make progress face sanctions.

NCLB exposed the dismal performance of schools. But it has also demonstrated how clumsy Washington's hand can be. A requirement for "highly qualified" teachers turns out to have helped keep states from hiring good ones. State standards diverge wildly. NCLB's main goal, for all pupils to be proficient in reading and maths by 2014, is unrealistic. And thanks to an odd way of judging schools, more than 80% may be labelled as "failing" this year.

Mr Obama has already offered one new model: dangle carrots for reform and hope that states bite. The stimulus offered more than $4 billion in grants for states that made certain changes, such as lifting caps on the number of charter schools and devising new ways to evaluate teachers. No state had to apply for the grant programme, Race to the Top, but 46 did.

With the new version of NCLB, Mr Obama can go further. He wants to set clear goals but give states more flexibility in meeting them. His plan would fix NCLB's most obvious failings, such as neglecting to track the progress of individual pupils. Only the worst schools would face dramatic intervention. Districts would evaluate teachers on a range of factors, including pupil performance.

Such plans would seem ripe for bipartisan compromise. Gene Wilhoit, director of the Council of Chief State School Officers, thinks that Mr Obama has moved in the right direction. Many of the president's priorities, such as improving teaching, overlap with those of conservatives.

But Republicans are wary. John Kline, the chairman of the House education committee, frets that states spend too much time complying with federal rules. Race to the Top had good goals, but poor implementation. He is dubious about the proposed interventions for failing schools-a concern he shares with the teachers' unions. Mr Kline's party now faces an awkward choice. If the Republicans pass a new version of NCLB, they will give Mr Obama a victory. But if they do nothing, Democrats will blame them for failing to fix a law that voters have come to hate.

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The birth of the New Deal

A blaze that galvanised the labour movement



No way out for many

THE fire at the Triangle Shirtwaist factory on March 25th 1911 began just before the end of the working day; some of the workers had already put on their hats. Escape routes were limited. One of the doors was locked and the New York fire brigade's ladders only reached the sixth storey, 30 feet (9 metres) short of the burning floors. Half an hour after the alarm, the fire was mostly out, but 146 people were dead. Most were women, many were in their teens and almost all were Jewish or Italian immigrants. More than 50 burned to death on the factory floor, 19 fell into the lift-shaft, at least 20 died when the overburdened fire escape broke free of the building and 53 jumped or fell from the windows.

Many of the horrified onlookers would have known that the Triangle had been part of a 20,000 strong citywide garment industry strike the previous year. New York's strikers wanted unionised workplaces, safer working conditions, better pay and shorter hours. But Triangle's owners would not allow the workers to unionise. The tragedy became a catalyst for a broad range of reforms. A state commission investigated the fire, but also took on issues such as low wages, long hours, child labour and safety.

Within a few years the city and the state had adopted 36 new laws, the country's most comprehensive labour rules and public-safety codes. They served as a model for other states and the New Deal's labour legislation of the 1930s. Frances Perkins, later Franklin Roosevelt's labour secretary, was one of those who watched the fire. She later called March 25th 1911 the day the New Deal began. Before the fire, unions tended to tackle owners individually. Afterwards, they had the law on their side.

Lee Adler, who teaches collective bargaining at Cornell University, sees parallels between the way the sweat-shop owners treated their workers and how a few governors in the Midwest are treating civil servants these days. The comparison is perhaps farfetched. But the anniversary does remind America why unions were needed. Last week 100,000 people

protested against the governor of Wisconsin's assault on public-sector collective bargaining. A hundred years ago 400,000 attended the memorial service for those who died, in part, because they could not unionise.

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Florida's budget

Austerity parade

Is Rick Scott cutting too deep?

ON MARCH 8th, at a rally in Orlando protesting the austere budget proposed by Rick Scott, Florida's governor, Alan Grayson, a former congressman, accused Mr Scott of wanting to turn Florida into Somalia-a place without a functioning government. At a rally in support of Mr Scott two days later a jazz band in front of the state capitol building in Tallahassee sung a boppy little number with a chorus of "Goo-goo, ga-ga, those Democrats cry like babies." So the propaganda war was probably a draw.

The real war will be harder fought. Florida faces a $3.6 billion shortfall in the coming fiscal year. That represents about 15% of the total 2011 state budget. Mr Scott, elected last autumn with strong tea-party support, has sharpened his axe. His budget cuts around $3.5 billion in government spending in the next fiscal year, as well as 8,930 state jobs and another 4,106 in the year after that. State employees will have to put 5% of their salaries into their retirement accounts (they currently pay nothing), and new state employees will have to take up 401(k)s (defined-contribution plans) instead of getting the defined-benefit pensions that have been a traditional perk in the public sector.

Mr Scott also proposes cutting Florida's property- and corporate-income tax rates-the latter from 5.5% to 3% next year-and then trimming it by 0.5% in each subsequent year, so that it will reach zero in seven years, by which time he aims to have created 700,000 new jobs in Florida. In his "state-of-the-state" address on March 8th, he said his budget "will give Florida a competitive edge in attracting jobs".

It may do that, though it also would cut education spending by $3 billion in a state that already ranks near the bottom in spending per head on education and has a high-school graduation rate well below the national average. It would lay off thousands of state workers, when Florida already has the fewest state employees per head of any state and an unemployment rate that, as of January, was 2.9 points above the national average. And it provides roughly $2 billion in tax cuts in a state that already levies no personal income tax, relies heavily on sales taxes and faces the waning of federal stimulus dollars.

It comes as no surprise that Democrats detest Mr Scott's budget. The more interesting question is how far he can count on Republican support. The president of Florida's Senate and the speaker of its House-both Republicans-are lukewarm about the proposed tax cuts, and his relations with his own party have often been rocky. In the primary he spent more than $30m of his own money to defeat Bill McCollum, the state's attorney-general and the Republican establishment favourite. In February Mr Scott came under fire from the (Republican) Senate budget chairman for selling two state aeroplanes and spending the proceeds without legislative approval. Earlier this month, a Republican senator sued him and many others rebuked him for rejecting $2.4 billion in federal funding for a high-speed railway line between Tampa and Orlando (the case was dismissed). Mr Scott, formerly the head of a company that ran hospitals, campaigned on the promise that he would run Florida like a business. But businessmen rarely have to contend with legislatures.

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Nuclear waste

From bombs to $800 handbags

Trouble stalks America's biggest clean-up



Where there's muck, there's brass

UNTIL the Japanese catastrophe of last weekend, the biggest nuclear mess in the Western world could be found at the Hanford nuclear facility in Washington state, where America's government once made most of the plutonium for its nuclear weapons. More than two decades after the clean-up began, officials have yet to deal with any of the nasty stuff.

At the Hanford site, which sprawls across a sagebrush plain in the south-east of the state, none of the 53m gallons (200m litres) of highly toxic waste stored in 177 ageing and leaky underground tanks has been mopped up, even though the last reactor was shut down in 1987. That must wait until 2019, when a unique waste-treatment plant-described as the largest and most expensive nuclear clean-up project ever undertaken-will begin transforming radioactive leftovers that could poison the nearby Columbia river into still-radioactive glass logs more suitable for long-term storage. If all goes well, gunk-to-glass processing ("vitrification") will continue until at least 2047 and cost about $74 billion, more than the annual budget of America's Department of Education.

But all is not well. The Defence Nuclear Facilities Safety Board, which watches how the Department of Energy runs its nuclear-weapons sites, is currently investigating the safety of the waste-treatment process itself. A whistleblower was removed from his senior job last year after warning that the plant could explode once the operation starts. The safety board is looking into the possibility that witnesses at a hearing were pressured by the DOE and its contractors to downplay the risks. The DOE, in response, has sent a peeved letter to the safety board. It insists that the plant will be safe and warns that the safety board has no authority to investigate possible witness tampering.

"The safety board is on a collision course with the DOE," reckons Robert Alvarez, now at the Institute for Policy Studies in Washington, DC, and formerly a DOE official who monitored Hanford. "It will raise uncertainty, lead to more delays and drive up the price of the clean-up." For local residents, this is not by any means bad news. Cost overruns and delays have plagued the clean-up-and the quarter-of-a-million people who live near Hanford are vastly richer because of them. "If the government spends more money, it is good for all of us," says Leonardo Luzi, the owner and chef at Bella Italia, a pricey eatery in the nearby town of Kennewick.

Thanks to Hanford's sustained ability to soak up federal dollars, the great recession skipped over Richland, Kennewick and Pasco, fast-growing towns on the Columbia river that call themselves the Tri-Cities. House values soared. Job growth in the area was, amazingly, the highest in the country last year. Environmental scientists earned higher salaries there than in Seattle. Business publications include the Tri-Cities on their lists of the best places to live and work. At the Columbia Mall, where it is often difficult to find a parking space, a Hallmark shop selling greeting cards was recently replaced by a Coach shop selling $800 handbags.

People in the area are still proud of having churned out 64 tons of plutonium over 40 years for America's tens of thousands of nukes. The material that went into Fat Man, the plutonium bomb detonated over Nagasaki, was made at Hanford, which at its peak consisted of nine nuclear reactors and five plutonium reprocessing plants. Richland High School still calls itself "the home of the bombers". A sign in front of the school features a mushroom cloud. But the local residents also understand that cleaning up after the cold war pays even better than winning it.

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Lexington

The courage factor

Has Barack Obama ever been brave? Perhaps more pertinently, will he ever be?



IT IS hard to see risk-free options for outside intervention in Libya. And as Colonel Muammar Qaddafi closes in on the pro-democracy rebels, Barack Obama, as is his wont, is erring on the side of caution; carefully considering, as he has for weeks, what, if anything, he ought to do. But this prompts a question about the president. Has he, at any point in his presidency so far, demonstrated real political courage? It is surprisingly hard, more than two years in, to think of an unambiguous example.

True, he went to the wire on health reform, but by the time he got round to doing so it would have been even riskier for him to accept defeat than to press forward. He spent nearly $1 trillion on economic stimulus and bailed out the car companies. But although they were controversial he had plenty of support for both decisions, which makes them bold rather than truly brave. If political courage is taking a clear stand against the majority on some gut instinct or principle, it is much easier to list the cases where Mr Obama has chosen discretion over valour.

He has left Guantanamo open, despite promising to close it. He reinforced the troops in Afghanistan, but set a date to start withdrawing, a careful bit of bet-hedging. He pushed for peace in Palestine, but retreated at the first whiff of domestic opposition. He created a bipartisan commission on the deficit, but then distanced himself from its recommendations. He said he would let the Bush-era tax cuts expire for the rich, but backed down after the mid-term elections. His support for gay rights has been a study in caution, like his position on gun control. He declined to criticise the treatment of Private Bradley Manning, the alleged WikiLeaks informant, whom the Marine Corps holds in solitary confinement and who has to stand naked outside his cell every morning. He fired an official who did speak out.

If Mr Obama is not brave, is he a coward? That is too harsh: politics, being the art of the possible, is not always about drawing a line and making a stand. Courage is a virtue in a president, but so are cool calculation and risk-aversion. If these are the president's dominant traits, some will say that they are a welcome corrective after the martial impetuosity of his predecessor.

Besides, one interpretation of that list is that Mr Obama is calculating, not craven. Guantanamo? While the terrorist threat continues, a case can be made that there is still a place for detention without trial. Palestine? Maybe the obstinacy of the local actors makes peace unattainable no matter how hard he pushes. Taming the deficit while the re-energised Republicans refuse to increase taxes looks nigh impossible; better, perhaps, to try again after his hoped-for re-election. Taxing the rich? Did he not have to back down once the Democrats lost the House of Representatives, and at least he extracted more spending on the poor from the Republicans in return. As for gay rights, he did eventually repeal the ban on gays serving openly in the military and is relaxing his opposition to gay marriage. On guns, he happens, conveniently, to agree with most Americans that the second amendment guarantees an individual right to bear arms-though he wants stronger efforts to keep guns out of dangerous hands.

The dream versus the calculation

In all these ways Mr Obama has clung to the middle ground, cutting deals where possible and sidestepping fights he judges he cannot win. It is all very practical, very realistic. But remember that he campaigned on the slogan that "we can". The fact that in so many instances he has not has deflated the ardent supporters who wanted a "transformational" president. The only people calling him that now are those absurd conservatives who claim he is transforming America into a secular-socialist dystopia.

Perhaps the expectations were the problem. Teddy Roosevelt thought presidents should "kindle the people with the fire from their own burning souls". In truth, few presidents change America all that much. That is the hemmed-in nature of the office, though voters habitually forget this. This "Cult of the Presidency" was explored brilliantly in a book of that name in 2008. Its author, Gene Healy, observed then that despite the disappointment of the Bush years, Americans were once again intoxicated by the aura of hope surrounding Mr Obama. He predicted that they would once again have cause to regret their infatuation with "the false promise of presidential power".

And so they have. In domestic politics especially, the president is checked and balanced at every turn. A British finance minister unveils his budget in the House of Commons and it is law. When Mr Obama sends his budget to Congress it is only pawn to king four: the opening move in a long game which the president has no guarantee of winning. This is the excuse his defenders offer to those who detect a want of courage in Mr Obama: he inherited a mess, his power is constrained and he has only reached the middle of the game. Have a heart, cut the man some slack. Sometimes, after all, discretion really is the better part of valour.

There is a danger here of letting Mr Obama off too lightly. He made hope and audacity his running mates, so he should answer for their defection. With the exception of health reform the big fights-on global warming, immigration and the deficit-have been put on hold and many of the smaller ones ducked.

Political courage is hard to define. But you know it when you see it. The senior George Bush increased taxes and paid with his job. Lyndon Johnson passed the Civil Rights Act even though he knew it would cost the Democrats the South. The much-maligned younger Mr Bush showed a moment of true grit, when he defied almost everyone and refused to leave Iraq to chaos in 2007. Maybe Mr Obama will find the same raw courage when at last he thinks it warranted. All one can say is that it has not happened yet. Meanwhile, Libya and Bahrain burn.

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The United States and Latin America

Flying down to Rio

Latin Americans like Barack Obama. They would like him even more if his rhetoric of partnership was matched by policy changes



IN APRIL 2009, shortly after becoming president of the United States, Barack Obama attended a 34-country Summit of the Americas in Trinidad where he charmed those present-even Venezuela's Hugo Chavez-with a call for the often fractious relationship between the United States and its neighbours to become an "equal partnership". Two years on Mr Obama remains wildly popular with ordinary Latin Americans. But as he sets off on March 19th for his first trip to South America, he will find it hard to shake off a familiar air of mutual frustration.

For a start, part of Mr Obama's mind will surely be elsewhere, on the wrangling in Washington over the budget and on the events in the Arab world and Japan. It must once have seemed a good idea to spend a weekend in Rio de Janeiro, watching a song-and-dance show in a *favela*. But to his domestic opponents it may not appear so.

For many South Americans, the United States is no longer the only game in town (if it ever was). Trade with China is booming. Many South American countries feel increasingly confident that they can make their own mark in the world. That is especially true of Brazil, the most important leg of Mr Obama's trip.

Relations between the two countries have long been beset by minor niggles. But last year saw a big falling-out over policy towards Iran. Brazil, along with Turkey, voted against the UN resolution that tightened sanctions against Iran's nuclear programme. Luiz Inacio Lula da Silva, Brazil's then president, had earlier tried to broker a deal with Iran.

Brazil's new president, Dilma Rousseff, is a protegee of Lula. But American diplomats are heartened by signs that she wants a fresh start. She has distanced herself from Iran, saying that she disagreed with Brazil's previous abstention on votes condemning the country's human-rights record. In a cabinet with many holdovers from Lula's day, one change stands out: Celso Amorim, who was closely associated with the Iranian adventure, has been replaced as foreign minister by Antonio Patriota, a former ambassador to the United States who is married to an American.

Mr Obama and Ms Rousseff have potentially important business to do. They will sign agreements on scientific co-operation and the cross-recognition of patents. They will also talk of weightier matters. Mr Obama will want to push business opportunities for American firms; the United States has a rising trade surplus with Brazil and the White House is selling the visit as part of its efforts to revive the economy. Although Ms Rousseff has postponed a $6 billion order for fighter jets, Mr Obama will press the merits of Boeing F-18s (rather than France's Rafale). The Brazilians want technology transferred in the eventual deal; they also want to sell to the Americans their own military-transport aircraft.

The Americans would like Brazil's backing for their calls for China to revalue the yuan, though Brazil's policymakers also blame the Federal Reserve's loose monetary policy for the overvaluation of the real. Brazil wants the United States to end its subsidy to its inefficient corn-ethanol producers. That would open the market for Brazil's sugar ethanol.

Brazil craves American support for its claim to a permanent seat on the UN Security Council. In November Mr Obama gave explicit backing to India's claim. But the mistrust sown by Lula's Iranian gambit means that the furthest the administration has gone is to say that it "admires" Brazil's "growing global leadership" and "aspiration" to the seat, as Hillary Clinton, the secretary of state, put it last month.

Mr Obama's next stop, in Chile, was to see an agreement on nuclear co-operation. But Chile, subject to earthquakes and tsunamis, is fast reconsidering the idea of nuclear power. Mr Obama's last stop is El Salvador. Its president, Mauricio Funes, is a moderate, pro-American leftist; and Central America is beset with drug violence.

In Santiago Mr Obama is to give a speech setting out his vision of relations with Latin America. It will not be easy. The issues that matter most south of the border are migration, curbing America's demand for drugs and export of guns, expanding trade and ending the American embargo against Cuba. On all of these the president is circumscribed by political deadlock in Washington.

The United States still matters in many ways in Latin America. Mr Obama's own story inspires many in a region where blacks and indigenous people are often disadvantaged. He can be a powerful voice for democracy and human rights. But unless his words are backed up with some substance his appeal may fade.

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Rebuilding Haiti

The long, hard haul

Can a presidential election change the hopelessness of the Haitian state?



A BIG sewage channel runs through Port-au-Prince, Haiti's capital, heading for the sea. If any of its raw sewage actually gets there, it can only dribble out. The channel is clogged deep with plastic bottles, garbage and human faeces. A video on the World Bank website shows a crane scooping it clean, removing rubbish "the size of a small mountain". But since no one has resolved the issue of why the channel was blocked in the first place, it is clogged up all over again.

More than a year after a 7.0-magnitude earthquake devastated the country, Haiti is still a mess. The chaos affects its politics, too. The first round of the presidential election, held in November, was marred by charges of fraud. An outside review found that the government's chosen candidate, who had been proclaimed the runner-up, had actually finished third.

He was removed from the run-off and replaced with Michel Martelly, a singer best known for a trouser-dropping routine, who recently admitted defaulting on over $1m of loans on property in Florida.

On March 20th voters will choose between Mr Martelly and Mirlande Manigat, a grandmotherly former first lady and legal scholar. Both are right-wingers. Ms Manigat's ties to the political establishment may hurt her, given Haitians' dissatisfaction with the slow pace of rebuilding. Recent polls give Mr Martelly an edge. "Only a bad boy can fix this country," said one recent caller to a local radio show.

The first order of business is organising a successful election. Some 500 poll workers were fired after the first round, and their replacements are supposedly better trained. The typeface on voter rolls will be bigger, too. Nonetheless, most residents of tent cities have no idea where they are supposed to vote. Any whiff of fraud could spark violent protests.

A further distraction is the impending arrival of Jean-Bertrand Aristide, a former president, who has announced that he will return from exile in South Africa before the vote. Mr Aristide was toppled by a rebellion in 2004. His opponents accuse him of ties to drug traffickers; many of the poor, however, still see him as their champion.

The turmoil surrounding the election risks delaying the hard work of reconstruction even further. Emergency aid operations certainly saved thousands, but all the aid agencies and all the money pledged cannot put Haiti together again. Only Haitians can do that.

Even a year later, no one knows how many died in the quake. The UN and most agencies think 222,570 were killed and 300,572 injured. But Jean-Max Bellerive, Haiti's prime minister, claims that the real death toll was 316,000. Others, more cynical, say this figure was bumped up so that it would be higher than those killed in the Indian Ocean tsunami of 2004. Big numbers bring more sympathy and more money.

Following the quake the United States and others rushed to bolster the 7,000 UN troops already there. Around 8,930 foreign soldiers now keep the peace, with 3,300 police to "stabilise" this chronically unstable country. All the big humanitarian aid agencies, plus thousands of small ones, piled in. To avoid muddle and duplication, they grouped themselves into "clusters" according to whether they were dealing with, for example, food, sanitation or water, and tried to work together. The result was encouraging. Within four months of the quake those who had lost their homes were under shelter, receiving food and chlorinated water.

Figures are unreliable, but UN data show that the peak of tent-dwelling was reached last July, when 1.5m people were packed into them. By January that figure was down to 810,000 in 1,150 camps. Yet even now massive tent camps still crowd into every available space in Port-au-Prince, nearby Leogane-the quake's epicentre-and other places. Many of those who remain under canvas will be far harder to shift than those who have already sorted themselves out. Perhaps 70% of them were previously renting their homes. So they have no house to rebuild, no land and no money anyway. They feel they are better where they are.

Ask people in these tent cities if they have been receiving regular aid and they will tend to tell you they have not. But, says Mr Bellerive, people always say that. He asked a woman he had seen receiving food the day before, who lives in a camp in the gardens of his quake-wrecked office, why she had said on television afterwards that she had received nothing. "Because it is the only way to make sure people will continue to help," she replied. Tent dwellers, used to journalists and do-gooding foreigners, are now well-aware that they can play to the media.

Better a tent than a slum



A large but unknown number of people in the camps are choosing to stay in them. Life is better there than in the sprawling, gang-infested slums. Camp-dwellers pay no rent. Nor do they have to pay for sanitation, because latrines are often provided by the aid agencies, or clean water, since that is often supplied by the agencies or by the government. Medical services are also easier to find and, again, probably free, courtesy of agencies like UNICEF or charities like Medecins Sans Frontieres. A cholera epidemic makes that all the more vital.

Nigel Fisher, who oversees the UN's aid operations in Haiti, worries about this. Haitians need permanent solutions, including jobs and education; but many now have no incentive to move. Aid is filling a gap that should be filled by the Haitian state. Unless the government can take charge again, properly providing for its people, Haiti will remain chronically and disastrously addicted to foreign aid.

Ever since Christopher Columbus landed on the island of Hispaniola in 1492, Haiti's history has been brutal. Its moment of glory came in 1804, when its former slaves founded the first independent black republic. Yet the violence of the revolution wrecked the country; Haiti also had to borrow to pay crippling reparations to France, the former colonial power: the loans were not paid off until 1947. Haiti's people lived under sanctions, isolated and oppressed by a succession of generals, dictators and bad rulers. Ever since 1804, laments Lorraine Mangones of FOKAL, a local NGO, Haiti has been unable to overcome its history and create a modern state.

Since the quake Haiti has received headline pledges of $10.2 billion in aid, including $1.1 billion in debt relief. Of this, under firmer promises, Haiti is supposed to receive $5.5 billion over three years. Mr Bellerive and Bill Clinton, former president of the United States, are in charge of deciding how and where much of the aid is disbursed. To date $1.28 billion has been paid out. But even the full $5.5 billion, divided among 10m Haitians, amounts to less than $185 a year per person.

Mr Bellerive also points out that at least 40% of any aid money goes on the salaries, insurance, cars and so on of the foreigners who come to hand it out. So aid alone can help, but it cannot fix Haiti. Unless development is co-ordinated by the government, it will not be sustainable.

Haiti is often mocked as "the Republic of NGOs". In the aftermath of the quake, says Mr Bellerive, the government was more or less ignored. Now it is trying to reassert control. That is far easier said than done-and not just because almost every government building was toppled, and nearly one in five civil servants died. One consequence of Haiti's poverty trap is that 84% of Haitians with more than a secondary education lived abroad in 2000, according to a study cited by the World Bank. How can the next Haitian government do even half of what it needs to do, if so many of the best and the brightest have fled?

And there is worse. According to Joel Boutroue, an aide to the prime minister, the Haitian government's reputation for incompetence and corruption means that foreigners no longer trust it. Although the government cannot operate unless it is reinforced with money and manpower, aid agencies constantly bypass it, condemning the state to stay forever weak.

Compared with many other big aid recipients, Haiti's government gets little direct budget support, says Mr Boutroue, sadly, "but it is far from being the most corrupt in the world."

Given enough resources and training, Haitians can work well. You need only look at the symbols spray-painted on almost 400,000 buildings across Port-au-Prince by Haitian engineers. The tags indicate that they have examined the buildings and determined whether they are safe, need repairing or should be demolished.

Yet the next stage of reconstruction will be crucial. The absence of a functioning government means there are no building regulations. Haitians tend to build walls with light concrete blocks which are not reinforced and they then use heavy concrete slabs for roofs and ceilings. Shake the walls and they crumble, so that the concrete falls and crushes anyone underneath. Much of what is now starting to be rebuilt may be as deadly as what was there before. And it is only a matter of time, say the experts, before another earthquake strikes.

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Life in rural Haiti

Goodbye, world

Why even Port-au-Prince seems a better place to be



A hellish kind of paradise

THE sea is warm and azure blue. Fishermen mend their nets under coconut palms, children play and music drifts from the church on the hill. It is a world away from teeming, violent Port-au-Prince. But even here life is nasty, and often short.

Deomoun, also spelled Dieu Moun, is hard to reach-its name is creole for Adieu-au-Monde, or Goodbye World. The quickest approach involves a 40-minute ride along the coast in a fishing boat with an outboard motor from the village of Marigot (which in turn is 45 minutes by road from the southern town of Jacmel).

The voyage to Marigot and back costs $3, which few can afford. So every day schoolchildren from Deomoun, some as young as four, make the journey to Marigot and back on foot, a five-hour round trip. Women go to market this way, often alone. Rapes are frequent, but the women see no point in reporting them.

Deomoun has no electricity, no school, no doctor, no priest and no police. If you are ill, you need to get to Marigot. If you are very ill, even that may not save your life.

Families eke out a living by growing what food they can and by fishing. But every year there are fewer fish. Trees on the surrounding hills, as everywhere in Haiti, have been chopped down for charcoal. When it rains hard, landslides sweep topsoil down to the sea. This pushes fish farther out, beyond the range of the fishermen's modest boats. There they may be scooped up illegally by richer fishermen, with bigger boats, from the neighbouring Dominican Republic. Haiti lacks coastguards to stop them.

Each year environmental degradation makes life a little harder for the people of Deomoun. Irregular rainfall and loss of topsoil means that the land produces less than before. So, over the years, more and more men have taken up fishing. To try and maintain their catch, more fishermen use nets with a finer mesh. As more smaller, younger fish get caught, there are even fewer fish than before.

The Haitian government is as good as absent from people's lives in Deomoun, and foreign aid agencies rarely show up. Caught in such a slow, relentless downward spiral, it becomes easier to understand why so many Haitians from the countryside would rather try their luck in the slums of Port-au-Prince.

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China

Don't worry, be happy

The government introduces the country's new mantra



THE pursuit of happiness, runs one of the most consequential sentences ever penned, is an unalienable right. That Jeffersonian sentiment seems to have influenced even China's normally strait-laced, rubber-stamp legislature, the National People's Congress (NPC), which has just wrapped up its annual session. Increasing happiness, officials now insist, is more important than increasing GDP. A new five-year plan adopted at the meeting has been hailed as a blueprint for a "happy China". The prime minister, Wen Jiabao, however, appeared downright miserable as he described the challenges he faces.

At the end of the ten-day meeting, Mr Wen told journalists that his remaining two years in office would be "no easier" than the preceding eight. Keeping the "tiger" of inflation in its cage would be hard enough, he said (the NPC approved a target of 4% this year, compared with inflation of nearly 5% in February). But corruption was the "greatest danger". A few days before the session began, the railways minister, Liu Zhijun, had been dismissed in connection with a huge bribe-taking scandal.

The five-year plan called for 7% annual average growth in GDP between now and 2015, compared with a far-exceeded target of 7.5% set in 2006-10. Mr Wen said lowering growth without raising unemployment would be an "extremely big test". But, he said, China had to change its pattern of economic growth, because it was (using a hallmark phrase) "unbalanced, unco-ordinated and unsustainable".

The idea of promoting happiness spread over the country like a huge grin early this year when provincial governments began laying out their own five-year plans. Guangdong province declared it would become "happy Guangdong". Beijing (which is a province-level administration) said it wanted its citizens to lead "happy and glorious lives". Chongqing municipality, another province-level area, said it wanted its people to be among the happiest in the country. Officials now often talk of setting up "happiness indices" by which government performance should be judged.

The word's popularity among bureaucrats is more an attempt to please leaders in Beijing and show sympathy for the less well-off than a sign of any real determination to change their ways. Many lower-level governments have continued to set investment-driven GDP-growth targets that are far higher than Mr Wen's. Some of his goals, such as building another 36m subsidised homes by 2015, will require the co-operation of local governments. They are adept at evading such tasks.

Mr Wen does not see political freedom as having much to do with happiness. In August last year he raised hopes among some liberal-minded intellectuals when he made a flurry of statements about the importance of political reform. Since then, the repression of dissidents has been stepped up. Dozens have been rounded up or put under surveillance in order to prevent them from responding to anonymous internet-circulated calls for an Arab-style "jasmine revolution" in China. To deter any protests, police security during the NPC was even heavier than usual.

At his press conference, Mr Wen repeated some of the language he had used last August on the need for political reform. This included a warning that China's economic gains could be wiped out if the country failed to reform politically. He also said people needed to be able to "criticise and supervise" the government. But he offered no guide to how this should happen, and stressed the need for change to be "gradual", "orderly" and "under the leadership of the party". He said it would be wrong to draw comparison between the situations in the Middle East and north Africa and that of China.

The NPC's chairman, Wu Bangguo, went further, telling delegates that the country faced an "abyss of internal disorder" if it strayed from the "correct political orientation". He also declared China had achieved its goal of setting up a "socialist legal system with Chinese characteristics". The Communist Party said in 1997 that it would do this by 2010, but never made it clear how progress would be assessed. China's struggling band of independent lawyers, who are often spurned by courts and harassed by police for trying to defend victims of official wrongdoing, are probably not celebrating.

The government's crackdown on dissent apparently includes a strengthening of China's internet firewall to make it more difficult to use software to evade blocks on sensitive foreign websites. Some websites in China recently carried a report that 11% of respondents to an opinion poll believed national happiness is boosted when they express themselves freely on the internet. If only they could.

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Pakistan

Money is thicker than blood

America and Pakistan agree to settle their spy dispute

NOT everyone will sleep easier after a Pakistani court freed Raymond Davis on March 16th. The American, a contractor who worked for the Central Intelligence Agency (CIA), had faced trial for killing two robbers on a busy street in Lahore late in January. There was no way to hush up the affair. Two others, also from the CIA, compounded the crime by knocking down and killing a third Pakistani as they raced to Mr Davis's aid. As it became obvious that the American was no ordinary diplomat-his car was jammed with extravagant bits of spy gear-anti-American street protests erupted.

Pakistan's main military-intelligence body, the ISI (Inter-Services Intelligence), kept the public mood simmering. It leaked telling details, such as the fact that Mr Davis had fired 12 bullets at his assailants, including three into the back of one victim. The ISI has been in a foul mood for months, angry that American spies have been allowed, independently, to hunt extremists such as Lashkar-e-Taiba (LeT), the group behind the 2008 Mumbai terror attacks, or the Haqqani network, which is behind a great deal of violence in Afghanistan.

American efforts to free their man plodded along slowly, hampered in part by politicians, notably the rulers of Punjab province, who were happy to milk anger on the street to bolster their own popularity. Neither the courts nor Pakistan's government dared to defy public anger (or the ISI) by accepting American claims that Mr Davis enjoyed immunity. That became irrelevant this week after the victims' relatives agreed to follow Islamic law and trade a pardon for cash (around $2m, in all, though the Americans denied paying). The families may also be relocated-which, if true, sounds like a wise move, since some extremists said they would kill anyone who took the Americans' money.

The relatives may have had limited say: a lawyer claims officials harangued them for hours to agree to the pardon. If so, what persuaded the officials? Rumours swirl that the Saudis may have acted as interlocutors. The heads of the CIA and ISI spoke recently by phone. The ISI had demanded oversight of those independent American agents and this week leaked the names of several dozen people who, agents or not, will probably now have to leave the country. More is the pity, if the upshot is less monitoring of groups like LeT, seen by Pakistan as useful, but by America as terrorists.

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Sri Lanka

The son also rises

Namal Rajapaksa, the president's eldest son, is being groomed for high office



Rajapak-son has some peculiar friends

DYNASTIES have to start somewhere. For an aspiring Gandhi in India, or a Bhutto in Pakistan, exploiting the family name to get into politics is relatively simple. Getting a dynasty going in the first place is more testing.

Sri Lanka's president since 2005, Mahinda Rajapaksa, is evidently giving the matter some thought. His government is already dominated by several Rajapaksa brothers, including a fierce one, Gotabaya, who oversees defence, and a more nimble-minded one, Basil, who runs economic policy. Now the 65 year-old president, who last month denied a rumour that he was being treated for cancer, is increasingly eager to promote his son, Namal Rajapaksa.

The 24-year-old MP is frequently taken on foreign trips by his father. In January he was dispatched to Libya to deliver a formal invitation for Muammar Qaddafi to visit Sri Lanka, to improve the "strong personal relationship" between the two country's leaders.

At home excuses are rustled up to keep him in the limelight. Last month he dispensed the man-of-the-match award at Sri Lanka's opening game of the cricket world cup, which took place in a newly built stadium in-by happy coincidence-his own constituency, Hambantota, in the south of the country. A few days earlier the portly young politician had been shown laying a foundation stone for a new office complex, funded by the Asian Development Bank; just before that he was named chairman of a new fund to protect a forest and an ancient pink quartz mountain range, the National Namal Uyana.

He is on hand to inaugurate new bridges and roads. As the head of a national body, Tharunyata Hetak ("aspiring youth"), he is whisked north-a chopper is usually on call-to dish out cash, books and other aid to victims of the civil war. His group has its own television channel, which shows him doing the dishing. He enjoys fawning-sorry, perceptive-coverage from state press and broadcasters.

His year-long political career has been charmed. His constituency, a Rajapaksa family stronghold since the 1930s, has been chosen as the site of a new international airport, a conference centre, hotels and other big projects. In November he officiated with his father at the opening of a large, Chinese-built harbour in Hambantota. Now young Mr Rajapaksa, charming, London-educated and fond of rugby, is leading a bid for Hambantota to host the 2018 Commonwealth games.

A presidential change will not happen overnight. Mr Rajapaksa *pere* remains popular among the Sinhalese majority for helping to force a decisive, brutal end to a civil war two years ago. He won a thumping re-election last year and has since pushed through constitutional changes that give him more clout and let him seek a third term, probably at an election in 2016. But preparing the son looks to be a form of insurance policy.

The opposition is hoping for a ruling family feud, as the son vies with his uncle to be heir-apparent (Basil had previously been touted as a successor). But Namal's promotion may suit the whole family. It must fend off accusations that thousands

of Tamil Tiger opponents and civilians were massacred at the dreadful climax of the war. Frequent foreign demands for an inquiry, and an attempt by the United Nations to launch one, have soured Western relations with Sri Lanka.

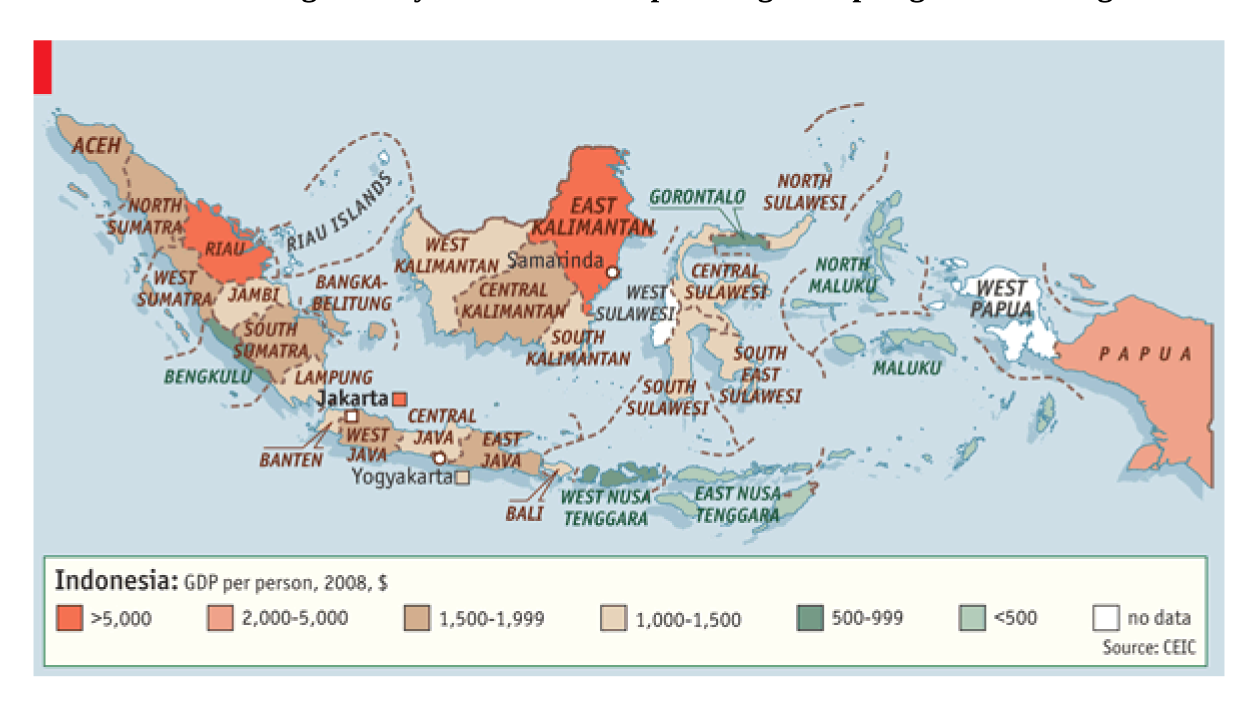
Patching up foreign ties and reconciliation with the aggrieved Tamils are the most important tasks facing Sri Lanka's rulers. These are much harder while Mahinda remains the face of government. If the Rajapaksas want a dynasty preserved for many years, preparing the way for a young insider, untainted by any role in the war, could be the family's canniest strategy.

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Indonesia

Power to the people! No, wait ...

Radical decentralisation has brought many benefits to the sprawling archipelago. But has it gone too far?



SHOCK and awe seems to be the purpose of the Utama Kaltim sports stadium. The four-tier, 50,000-seat showpiece rears out of the jungle, surrounded by 46 hectares of swimming pools and badminton halls. It would grace any of the world's big cities-but happens to be in a clearing outside the rather less well-known Samarinda, provincial capital of East Kalimantan on the island of Borneo. It has become a symbol of everything that has gone wrong with Indonesia's well-meaning plans to devolve power from the capital, Jakarta, to local and provincial governments.

From a distance the stadium oozes self-confidence and civic pride. It cost a whopping 5 trillion rupiah ($568m), paid for by the provincial government. The governor himself takes pride in it. But a pitchside inspection tells a sadder story. A weary groundsman is attacking knee-high weeds with a flymo under the hot sun. The last big soccer match here was played in May 2010. It is less a field of dreams than a backyard of disappointments. Waste on this scale, critics complain, is symptomatic of a decentralisation programme that is out of control. Some disillusioned Indonesians even contemplate the unthinkable: a U-turn, back to more central control.

Decentralisation began with high hopes in 1999 to reverse the extreme centralisation of the Suharto years. The dictator had tried to rule Indonesia's millions of people (now 237m) and its 17,000 islands with an iron fist from Jakarta. This provoked resentment and insurrection in resource-rich provinces such as Aceh, which saw their wealth plundered by a corrupt elite. There was even talk of secession in East Kalimantan, with its abundance of coal, gold, oil and gas.

After Suharto was toppled in 1998, the central government offered block grants and tax-raising powers to the provinces and local districts, providing them with the means to run their own affairs. Local leaders were to be directly elected every

five years. Anyone was allowed to petition the central government to create new units of local government. Unsurprisingly, given the money on offer, this has led to what Indonesians refer to as a "blossoming" of devolved authorities. In 1999 there were 292 districts in 26 provinces. Today that has grown to over 500 districts in 33 provinces.

In some ways, it has been a success. The country has held together. Devolution's boosters claim that "unity in diversity" is a reality. True, tensions remain between Jakarta and Papua, which is virtually a sealed state run by the army. But places like East Kalimantan are now proudly local and proudly Indonesian.

Many districts and provinces are also well run, especially on the most populous island, Java. Herry Zudianto, the mayor of Yogyakarta, the cultural capital of Java, is coming towards the end of a successful second term of office. He has streamlined the local bureaucracy, put every child in school and opened his office to anyone who wants to make a complaint.

Democrazy at work

But Mr Zudianto is the exception not the rule. Given the rewards on offer for a successful local politician-free money from the centre and the power to raise local taxes-perhaps it is not surprising that local electoral politics has become mired in corruption. Prospective candidates rack up big debts to bribe voters and political parties. Then, they resort to embezzlement in office to pay the debts. According to the government, up to the end of last year 158 district and provincial leaders had been charged with corruption, about a quarter of the total. Many of those have been jailed. Most of the guilty have been defrauding budgets and marking up the value of government contracts.

Money-politics now seems to be endemic. In the run-up to the first election in yet another new district earlier this year, one academic, Effendi Ghazali, was invited onto a local radio talk show to offer a bit of civic education. He found that most of those phoning in only wanted to know whether to accept bribes of up to $110 to vote, a lot of money in a poor part of the country. Candidates are increasingly resorting to intimidation to win. The International Crisis Group detected 20 violent incidents in the 200 or so regional elections held in 2010. That may not sound like many, but it was seven more than during all the elections from 2005 to 2008.

Then comes the sheer waste and inefficiency. Too often local leaders resort to bread and circuses to keep themselves in office. Indonesians have known about the empty stadiums and grandiose governors' mansions for a while. Now they are finding out about the huge sums local politicians extract from "social" or "sports" budgets to finance the local soccer teams.

East Kalimantan, for example, spent 11 billion rupiah on the local team last year, even forking out on players from Mexico, Argentina and South Korea. The success of the team will doubtless burnish the reputation of local politicians among a vital group of voters, young males. But is this a better use of taxpayers' money than schoolbooks or clinics in what is still a poor country? Even Mr Zudianto is spending 5 billion rupiah on the local Yogyakarta team, though he draws the line at buying expensive foreign players.

Critics argue that this is what happens when local politicians are given their head, when, as one senior politician puts it, you go "democrazy". There are hundreds of elections a year, but little or no supervision. There is a central anti-corruption agency, but it is weak at local levels.

As a result, the government has been cautiously floating ideas on how to rein in local autonomy. One is to have governors elected by provincial assemblies rather than directly, saving money on elections and perhaps reducing the scope for fraud. Another proposal is to increase the centre's powers of financial oversight.

But it will be an uphill task. Indonesians have come to cherish their local freedoms, with good cause-even if it means a white-elephant stadium or three.

Correction: An earlier version of this article identified Yogyakarta as Java's second-largest city, which it is not. This was corrected on March 18th, 1011.

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Banyan

Japan and the uses of adversity

The rest of Asia watches with horror, pity and admiration



FEW bright spots illuminate the bleak sequence of calamities unfolding in Japan. But here are two: the quotidian, stoic heroism with which so many Japanese have responded to devastating loss and terrifying danger; and the outpouring of sympathy and support for them from around the world. In the many parts of Asia where anti-Japanese sentiment runs deep, the disasters may even mark a turning-point in attitudes, bringing a new respect and warmth to perceptions of Japan.

Hostility towards the country in what bankers call "ex-Japan Asia" has fluctuated, and, especially in China, has at times been manipulated by governments. But it has never vanished. It has three roots. One is the legacy of Japan's imperialist past and its begrudging, half-hearted apologies for wartime atrocities. Second are simmering territorial disputes with China, Taiwan and South Korea over tiny islets in the East China Sea, and the fisheries and oil-and-gas fields around them.

Third is plain envy of Japan's efficiency, wealth and power, mixed with resentment at the arrogance they are sometimes seen as fostering. That Japan is a huge aid donor and investor in developing Asia has mitigated but not eradicated these prejudices, which have also withstood two decades of economic stagnation punctuated by a huge disaster-the Kobe earthquake of 1995. Japan's present emergency, however, may have a more lasting impact. It is more multifaceted and comes after a further 16 years of relative Japanese decline, including its recent ceding to China of its status as the world's second-largest economy.

Even now there have been a few vile, jubilant voices among Japan's neighbours. The chinaSMACK website reported a microblogger who greeted the earthquake with the pithy remark: "Splendid!" A blogger in Taiwan-an assistant to a member of parliament-criticised donations to Japan, and indulged in racist abuse of Japanese "dogs". Less grotesquely, a Malaysian newspaper published an insensitive cartoon of a popular Japanese *manga* hero, Ultraman, fleeing a tsunami.

All of this, however, met fierce criticism. One comment on the Chinese "Splendid!" post was "What's wrong with you?" The Taiwanese blogger's boss and the Malaysian newspaper were quick to apologise. And the cruelty was not just an Asian phenomenon. There was equally offensive rubbish on Facebook out of America, calling the catastrophes retribution for a 70-year-old act of infamy at Pearl Harbour.

Away from the nastier fringes of the internet, the typical reaction, in Asia as elsewhere, has been of appalled sympathy. As the tsunami of sludge swept over north-eastern Honshu on March 11th crowds gathered, transfixed by the pictures, in front of television sets in shops, bars, stations and airports. Since then it has become more apparent how many lives might have been lost, what hardship survivors are enduring, and what peril they face from the risk of a deadly nuclear disaster. Japan's past hardly seems relevant any more, except for the memory that it is the only nation to have suffered nuclear attack.

Beyond pity at seeing residents of a rich, proud country scavenging for food, hoarding bottled water and huddling for shelter on schoolroom floors, it was hard not to feel admiration as well. Chinese and Indian websites were agog at the orderliness of the Japanese, even those now homeless and even as the nuclear panic mounted. They noted the lack of looting. Some drew unfavourable comparisons with their own people and governments. An article on one Chinese site, *Caixin*, referred both to the earthquake in China's Sichuan province in 2008, when some 70,000 people died, and to the way schools in Japan have been used as shelters. In the Sichuan earthquake many schools collapsed. Parents blamed corruption and shoddy construction.

This popular response was matched by official warmth. Like China's during the relief effort that followed the Sichuan earthquake, Japan's foreign relations have improved. It has been on bad terms with China since a row last September over the Senkaku islands. But China has donated aid and, at his annual press conference on March 14th, Wen Jiabao, the prime minister, made a point of giving a message of support for Japan, recalling its help to China in 2008. Similarly, the disasters have led to a rapprochement with Russia, with which relations have also been fraught over a territorial dispute. Vladimir Putin, the Russian prime minister, has offered aid in the form of energy and ordered officials to speed up an oil-and-gas project on the island of Sakhalin to meet future Japanese demand.

Russia's offer may be based on the assumption that Japan will have to pare back its reliance on nuclear energy. And that is another lesson that Asian observers of Japan's crisis have taken home: if even Japan-so well-organised and disciplined, so well prepared for disaster and so experienced in nuclear power-can come so close to catastrophe, what nuclear risks are their own countries running? Despite criticism of Japan's handling of the nuclear crisis, many Chinese or Indians suspect their own authorities are no more competent or transparent.

Meltdown

Yet China is building almost as many nuclear power plants as the rest of the world combined. India, too, has big plans to expand its nuclear-power industry. Like China and Japan, it is prone to earthquakes. This week both India and China announced safety reviews. Neither is likely to call a permanent halt to further expansion. The world has tended to approve of their plans. Both countries at present rely heavily on coal for electricity generation, which both will be boosting hugely in coming decades. The alternative to nuclear expansion may be more coal, and higher carbon emissions. It is hard to look on the bright side for long.

Economist.com/blogs/banyan

Libya's uprising

The colonel charges ahead

In going after the rebels, suddenly Muammar Qaddafi is winning



GREEN banners that symbolise the rule of Muammar Qaddafi have returned to Libyan towns, many of them in ruins, where troops loyal to the dictator have chased away poorly armed rebels. Regional and Western powers quibble over how to stop the bloodshed, while the self-styled colonel is making great strides towards suppressing the month-old revolt.

On battlegrounds across the vast, empty land, his forces have taken back Zawiya and Zuwara west of the capital, Tripoli. They have tightened their siege of Misrata, 210km (130 miles) to its east, and pushed into rebel strongholds along the coastline. With their bigger guns, heavier armour and a monopoly on air power, they have captured oil facilities at Ras Lanuf and Brega, and seized a strategic road junction at Ajdabiya. In their sights is the eastern capital, Benghazi, stronghold of the rebel forces. If this city of 1m fell, Colonel Qaddafi would be free to hunt down the "rats" who have challenged his rule.

Yet the demise of the rebels is not assured. Across open desert and through small towns, loyalist advances have been swift. In urban areas, though, they have been far slower. The looming invasions of Benghazi and Misrata, another big city, may cost the loyalists heavily in men and materiel, for the defenders have no way of escape. But if the indiscriminate methods loyalists used to retake smaller towns are a guide, the toll on civilian life will also be grim. Already, world opinion scorns Colonel Qaddafi. On March 12th the Arab League endorsed the imposition of a no-fly zone over Libya. Western nations are facing mounting public pressure to intervene. Despite popular wariness about becoming enmeshed in yet another Muslim country, a fresh humanitarian crisis may tip opinion in favour of more punishing action against Libya's leader.

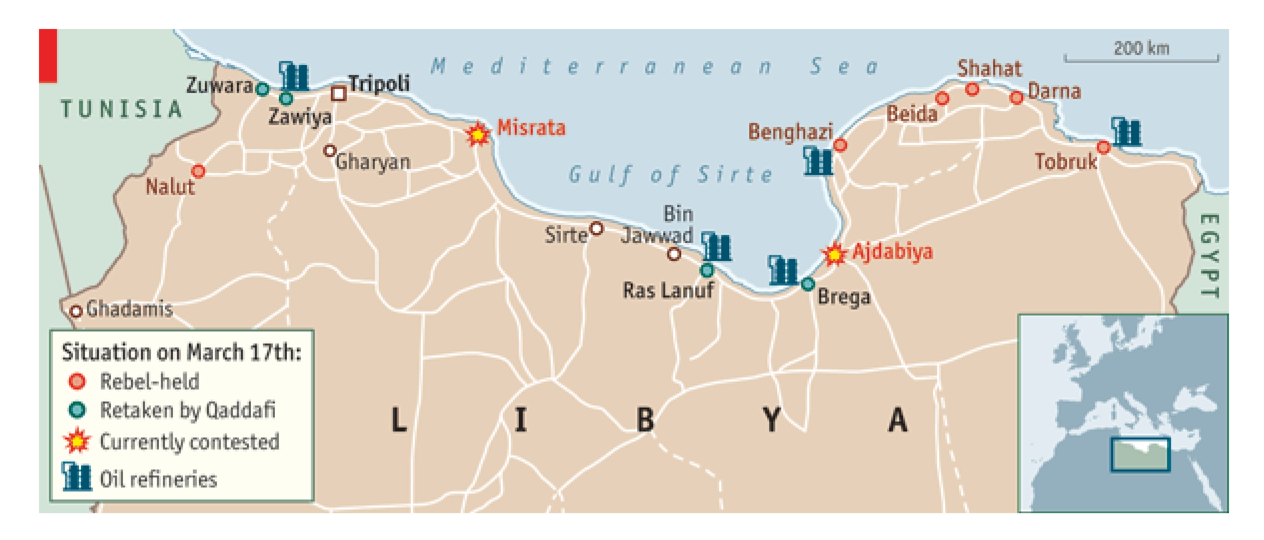
On March 13th, when a satellite news channel claimed, wrongly, that rebel forces had turned the tide with a night-time ambush, Benghazi residents declared that the only thing stopping them from attacking Tripoli was Colonel Qaddafi's air force. "If they imposed a no-fly zone, all of us would go and fight," says one unemployed youth looking at pictures of "martyrs" in what has become an open-air museum of the revolution outside Benghazi's courthouse. Would-be revolutionaries say they can attack tanks with the many rocket launchers found in Colonel Qaddafi's arsenals in the east. But they fear his planes circling overhead are out to bomb them.

Bravado in the face of repeated setbacks seems to be shared by the public. "Sawfa nabqa huna" ("We will remain here"), an anthem of Islamic resistance popular throughout the Arab world, rings out from loudspeakers and mobile phones. Asked about the danger of losing control of Benghazi, residents rattle off a list of uprisings they have staged over the four decades of Colonel Qaddafi's rule. "He was afraid of Benghazi even before we had weapons," says a lorry driver whose brother died in a massacre in 1996.

Street-fighting for beginners

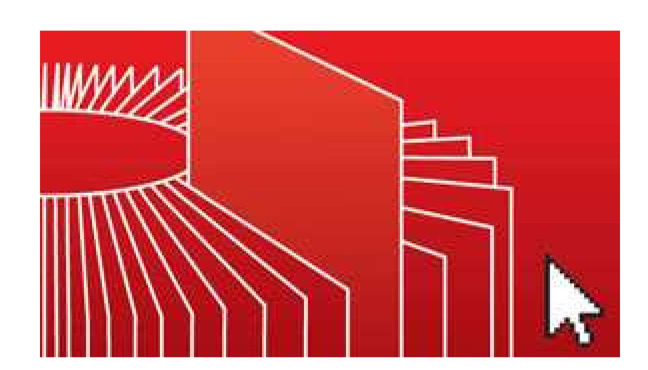
Benghazi is flooded with looted weapons and, with Colonel Qaddafi's forces knocking at the door, new owners are learning how to use them. A stretch of road outside one former army base, which offers target practice to anyone who walks in, was packed with cars. Moneim, a burly university student, says he is "taking the opportunity" of the fighting around Ajdabiya to learn how to use a rifle. He was not expecting Colonel Qaddafi to reach Benghazi, he said, but wanted a few street-fighting skills under his belt just in case.

The population's swagger may in part stem from the city authorities' capacity to keep up a sense that all is normal. The power is on, and in the city's bakeries sacks of flour are piled up to the ceiling. All may change if Colonel Qaddafi can move his forces to the outskirts of Benghazi even if he does not attack the city directly. One engineer from Brega, which provides the gas for the plants near Ajdabiya that power Benghazi, says an advance along the coast might force the east to fall back on diesel generators, which are laborious to supply, or take their power from the Egyptian grid for electricity. But none of those fallback plans will work if Colonel Qaddafi's troops swoop around the city to cut the roads leading to the Egyptian border, as they appear to have done in the west.



The opposition's biggest problem is a dearth of experienced forces, which are needed to keep supply lines open. Most rebel fighters are *shabab* (youth in Arabic), spirited but untrained volunteers, lacking any command structure and prone to headlong rushes and retreats down exposed roads. A handful of colonels have organised ad hoc forces of veterans. But military defections in the east that accompanied the revolution have not yielded any mechanised units or operational aircraft, or at least none that might leave their bases. Staff officers sitting around Benghazi's military headquarters say that Colonel Qaddafi took the families of unit commanders and other officers hostage and flew them west as soon as eastern towns fell, thus paralysing his mutinous army.

Mustapha Gheriani, speaking for the rebels' interim council, insists that the answer to their military woes is a no-fly zone. Failure to impose one, he says, will lead Libyan youth to conclude that the West has failed them. "These people will become a fertile ground for extremist recruitment."



Meanwhile, as Colonel Qaddafi's forces approach, his partisans in the city have become more active. Some rebel officials say their nascent security services warned known members of Colonel Qaddafi's "revolutionary committees" to stay indoors, and may be beginning to round up troublemakers. But the rebels' reach is limited. On March 12th, presumed regime loyalists ambushed and killed a cameraman for Al Jazeera, the broadcaster whose stirring montages of pan-Arab revolutions are blamed by regimes throughout the region for firing up opposition movements. Two days later another car of gunmen ambushed a youth just back from the front. "They call this a revolution?" says his brother bitterly. "Everyone has guns and no control." For a revolution, that sounds about right.

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Bahrain's crisis

Calling in the big guns

Security forces from neighbouring countries are joining an escalating crackdown



THE small Gulf monarchy of Bahrain has rapidly turned from an oasis of relative liberalism, where Saudis go to drink at weekends, to a country under a state of emergency where Saudi and Emirati troops are helping the government to quell unrest-none too tenderly. Reinforcements rolled across the border in a televised show of force on March 14th, stiffening the resolve of Bahrain's troops.

Together they violently removed protesters demanding political reforms from public areas in Manama, the capital, and destroyed their encampment in the city centre. Human-rights groups said that at least six protesters were shot dead. Three policemen were also reported to have been killed. According to witnesses, armed forces surrounded the main hospital at Salmaniya, as well as medical centres in Shia villages, perhaps to prevent the injured from receiving treatment; some doctors are apparently carrying out their work in private homes. The financial district, normally a sleepy version of Dubai, is now moribund as Western expatriates have fled.

In different parts of the small country vigilante groups have set up roadblocks and taken up makeshift arms, often on a sectarian basis. The mostly Shia village of Sitra has seen severe clashes between protesters and police. Facebook and YouTube are filled with photos of bloody corpses and videos of street fights. Two government ministers have resigned in protest.

The dispatch of some 2,000 Sunni forces from Saudi Arabia and the United Arab Emirates (UAE) to a majority Shia country has exacerbated sectarian tensions. The main Shia party has called it an "invasion", whereas many Sunnis see it as a "brotherly" intervention to restore order. Regionally, the move has been fiercely criticised by the Iranian president, Mahmoud Ahmadinejad, the leader of Hizbullah, Hassan Nasrallah, and the radical Iraqi cleric, Muqtada al-Sadr. That is probably the last thing the protesters need. All along they have said they are aiming for democracy and reform, not a sectarian agenda. The Saudi and Emirati forces have arrived under the banner of the Gulf Co-operation Council, a club of six Sunni monarchies, which has a collective-defence pact to fend off external aggression. It is the first time it has been used to protect a member from its own people.

Officially the troops are under the command of the Bahraini king while they are on his territory. But Saudi Arabia and the UAE are bigger, richer and more powerful, and it is not clear how much choice the Bahraini government really had in the matter. Its leaders depend on Saudi goodwill for oil supplies, which come from a shared offshore field administered by the Saudis and which provides the vast majority of the government's revenue. Bahrain, like Oman, has just been promised $1 billion of aid per year over the next decade from its wealthier Gulf neighbours.

American officials say they had little warning of the troop influx. It came just after Robert Gates made a visit to Bahrain in which he emphasised the need for far-reaching political reforms, saying that if the country wanted to keep its Shia population out of Iran's orbit, it needed to bring them into the political process.

For their part, many opposition members are convinced that the Americans gave the green light, and argue they are therefore complicit in the killing of protesters. This could encourage attacks on the US Navy's Fifth Fleet, which is based in Bahrain. It is possible that Saudi Arabia and the UAE made the decision to intervene on their own, angered by America's withdrawal of support for the former Egyptian president, Hosni Mubarak, a key ally. Neither country wants to see a wave of democratisation sweeping the Middle East. But both can probably assume that President Barack Obama will bite his tongue and continue to support them.

Yemen's demonstrations

Yet more cracking down

The police fires live rounds at protesters



Fight another day

GUNSHOTS rang out in the streets outside Sana'a University in the Yemeni capital on March 12th. Giant water cannons spat arcs of white foam through the early morning air as unarmed young men charged towards police in riot gear, shouting "irhal" (get out). Choking from the tear gas fired into the crowd, some hoisted sledgehammers to smash up the pavement in order to hurl broken slabs over improvised barricades that now enclose a makeshift camp. There, they say, they will stay until Yemen's president of 32 years, Ali Abdullah Saleh, steps down.

Yemen's anti-government demonstrators have become much more violent and have spread further across the country. The governor of impoverished Marib province was stabbed in a clash with anti-government protesters. In the even poorer al-Jawf district in the country's tribal north, security forces reportedly opened fire on demonstrators, injuring 15. Far to the west, police wounded dozens more with live fire in the port city of Hodeida, while large crowds marched in the central cities of Ibb and Taizz. In the south protests against Mr Saleh have strengthened a long-running independence movement. Each day brings a new toll of injuries from street clashes with police.

The anti-government demonstrators in Sana'a have extended their month-old camp outside the university into the neighbouring streets, setting up internet connections and screens showing satellite television. A handwritten sign in English reads: "Al Jazeera is part of our revolution." On March 14th four foreign journalists including this correspondent were detained and then deported. The few foreigners left in Yemen are either making plans to leave or are stockpiling food. The British ambassador has warned expatriates that Yemen may follow the path of Libya rather than Egypt or Tunisia.

Mr Saleh says he has told his security men to use force only in self-defence. So far it might be argued that they have shown at least some restraint. But as the opposition grows bolder, Mr Saleh is resorting to hired thugs and armed tribesmen to assault protesters across the country.



Government officials are quietly asking for help from foreign governments. The Gulf states could mediate. An intervention led by Saudi Arabia has been discussed, amid rumours that military aid is already flowing to Mr Saleh's forces. One Yemeni analyst emphasised the sway Saudi Arabia holds over Yemen's tribal leaders.

But the anti-government protesters insist they want Mr Saleh to go. "If we could ask him to resign yesterday, we would," says Khalid Al-Anisi, a prominent human-rights activist. He has suspended his membership in an Islamist opposition party, Islah, to throw in his lot with the students at the university in Sana'a.

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The Arab press

Read all about it

Like the region's politics, its newspapers face dramatic change

"THE cannibal has escaped from his hideout." "Bonaparte is advancing at a great pace but will never enter Paris." "His Imperial Majesty yesterday entered the Tuileries, among his faithful subjects." In 1815 it took just 13 days for *Le Moniteur*, a French newspaper, to go from demonising Napoleon to glorifying him. *Al-Ahram*, Egypt's leading newspaper, state-owned and long seen as a mealy-mouthed apologist for the regime, took only a few days longer to perform its own U-turn. On January 26th, after violent clashes between police and protesters in Cairo's Tahrir Square, the front page led with a fluffy story about flowers and chocolates being given to the police on their national day. By February 12th, the day after Hosni Mubarak had abandoned his post as president, the paper was singing a new tune. "The people have brought down the regime", it declared, applauding Egypt's youth for Mr Mubarak's removal. Was it an opportunistic *volte-face* or were long-repressed journalists delighted to throw off the shackles of censorship? Probably a bit of both. Either way it reflected the dramatic changes in the Arab fourth estate.

The Middle East has had a dismal record in press freedom. In a ranking of 178 countries by Reporters Without Borders, a Paris-based lobby, three of the bottom ten-Syria, Sudan and Yemen-are in the region. During recent protests, reporters have been attacked and locked up by security forces in Algeria, Egypt, Iraq, Yemen and beyond.

Al Jazeera, the Qatar-based satellite news channel, has dashed ahead of newspapers in covering the unrest. It has more money and more reporters. Few Arab newspapers have carried first-hand reports from eastern Libya, where Muammar Qaddafi has been ousted. Television presents a potent challenge to newspapers in a region plagued by illiteracy. But newspapers remain powerful opinion-makers, especially among the elites.

The region's doughty band of genuinely independent newspapers, long critical of governments, have faced fewer dilemmas. They marvelled at the protests in Tunisia, wondering if they dared to dream that this was the beginning of a new era. They wrote of their tears of joy at the sight of an Egypt reborn in Tahrir Square.

It has been a lot trickier for publications that are owned by (or are cosy with) those same regimes. Journalists at *Al-Ahram* have demanded the resignation of the editor-in-chief, protesting at his hypocrisy and calling for a new beginning. *Quryna*, a Libyan newspaper based in rebel-held Benghazi, Libya's second city, has long been close to the regime. It has now changed both its name and its politics. Under a new moniker, *Barniq*, it claims to offer something closer to objective

reporting. But the fact that it carries the new flag hoisted all over the east by the rebels suggests that it may just have switched allegiances.

In the Gulf, newspapers are playing a careful game. They are torn between placating their readers by calling for political change, and currying favour with masters who are twitchy about unrest. One Saudi daily, *Al Watan*, praised King Abdullah for being reformist while blaming his government for stifling reform. It made sure to report people's joy at the wodges of cash handed out by the Saudi king in February.

The Arab press in exile is also torn. The two most prominent pan-Arab papers published in London, *Al-Sharq Al-Awsat* and *Al-Hayat*, are owned by members of the Saudi royal family. Yet even their pages have run editorials rejoicing in the disposing of despots and dreams of democracy. The bad blood between Saudi Arabia and Libya over an alleged plot to assassinate the then Crown Prince Abdullah makes criticism of Colonel Qaddafi easier.

In the past Arab newspapers not owned by governments have been wary of crossing "red lines". Ahmed Ragab, a journalist at *Al-Masry Al-Youm*, an independent Egyptian paper known for its criticism of the Mubarak regime, says that before the revolution he was working under threats from businessmen and figures within the regime. Those threats are now gone. "But after 30 years of oppression, journalists are afraid of their own shadows." Self-censorship has become ingrained, and overcoming that will take a while. Moreover, it is no longer so obvious who is calling the shots. Government-owned papers like *Al-Ahram* will no doubt remain close to the regime, but perhaps less slavishly so.

Newspapers owned by the state will have to raise their game. The Egyptian government has three big dailies, myriad minor rags and various magazines to its name; in a democracy, many of these may expect to die. *Al-Ahram* has been massively subsidised and has at least 1,000 journalists working for it.

In a 2008 survey of 600 journalists across the Arab world by the American University in Cairo, three-quarters said they thought the point of journalism was to promote political and social change. Newspapers may not have caused the revolutions across the Middle East. But they will play a part in what comes next.

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Fighting in Cote d'Ivoire

Shifting lines

A former rebel army from the north gains ground, and may take the capital



The road to democracy

CISSE SINDOU, a senior member of the New Forces (FN) in Bouake, Cote d'Ivoire's second biggest town, is dressed in flowing royal-blue robes, relaxed, confident and smiling. For good reason. The former rebel army, which is now backing Alassane Ouattara, recognised abroad as the winner of November's presidential elections, has chalked up some big victories. They have both come in the west of the country, previously loyal to Laurent Gbagbo, the former but so far immovable president, and in Abidjan, the commercial capital on the Atlantic coast.

"We don't want war," insists Mr Sindou, who previously ran two restaurants in New York. "But the time will come when we must take matters into our own hands." He and other rebels, including groups of exiles, are waiting for Mr Ouattara's instructions. Though they claim to want to give peace a chance, a signal to move on the capital could come any day.

Meanwhile, a defiant Mr Gbagbo, holed up in the presidential palace a stone's throw away from his rival, clings tenaciously to power. In recent days dozens of corpses have been found in the streets, raising the death toll to 400. Mr Ouattara blames the killings on the former president. But this week Human Rights Watch in New York said both sides have committed atrocities.

The two sides can be hard to tell apart. On the sweltering main road from Abidjan to Bouake, checkpoints are manned by troops in identical uniforms-red berets and camouflage fatigues. Some are official forces, others are former rebels. All are similarly unsmiling, aggressively demanding money.

The FN these days prefers to be known as the Republican Forces: it sounds more inclusive. They have held the mainly Muslim northern half of the country since the civil war of 2002-03, following a failed coup against Mr Gbagbo, a Catholic, who had seized power two years earlier. But this is no ethnic or regional conflict. Support for Mr Ouattara, once a high-flyer at the IMF, cuts across many divides. The November election was meant to break the stalemate, yet deepened it instead. The country's economic life is slowly grinding to a halt. Banks have been closed for a month. People are running out of cash to pay for food, medicine and electricity.

Western economic sanctions are beginning to bite. The two main ports of the world's biggest producer of cocoa are nearly at a standstill. So is Cote d'Ivoire's only oil refinery. Cooking gas has already run out. The same will happen soon to petrol supplies. The streets of Abidjan are increasingly deserted, as people board up shops, homes and restaurants and flee the city before the coming battle. Everyone is waiting to see what happens next. No one expects Mr Gbagbo to go quietly.

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Corruption in Sierra Leone

Rich pickings

Bad apples are still in the barrel

AT LUMLEY JUNCTION in Sierra Leone's capital, Freetown, where Land Cruisers driven by foreign aid workers zoom past on Saturday mornings on their way to the beach, a large hoarding has, until recently, stood under a palm tree. "Attitude is Everything", it read. "Invest in Your Future by Changing Your Attitude and Behaviour for the Good of All Sierra Leoneans". Alongside stood a picture of President Ernest Bai Koroma, who set up an "Attitudinal and Behavioural Change Secretariat" after coming to power in 2007. Embarrassingly for him, Sierra Leone's Anti-Corruption Commission (ACC) has now indicted several of the secretariat's senior people, accusing them of siphoning off donated funds. So the hoarding has been hurriedly removed.

Sierra Leone's budget is a tiny $500m a year, but its leaders still enjoy rich pickings. A recent WikiLeaks cable suggested that senior military men had squandered an aid grant worth $1.9m from Britain on plasma-screen televisions and hunting rifles. "If you have been here for some time, you will know that anybody and everybody is stealing everything," claims Desmond Luke, an Oxford-educated former chief justice of Sierra Leone.

Sierra Leone's status as a model for post-conflict recovery has had an insidious effect on its bureaucrats, many of whom waste a lot of time inveigling themselves into delegations to conferences and seminars abroad, where they receive handsome allowances.

But at least some of the news is good. Laws passed in 2008 have bolstered the ACC. It is now free to prosecute cases itself rather than lay them before the attorney-general, who may ignore them. But the ACC recently annoyed anti-corruption campaigners by settling a scandal over the state social-security agency out of court.

In Freetown many people greeted the indictment of the attitudinal-change officials as a joke. Others were less amused. One of the accused was once a spokesman for a particularly nasty military junta. His reappearance may suggest that, nine years after the end of the bloody civil war, Sierra Leone has yet to rid itself of bad apples from a previous era. The new hoarding that replaced the one on Lumley Junction now celebrates the 50th anniversary of Sierra Leone's independence, which comes up in April.

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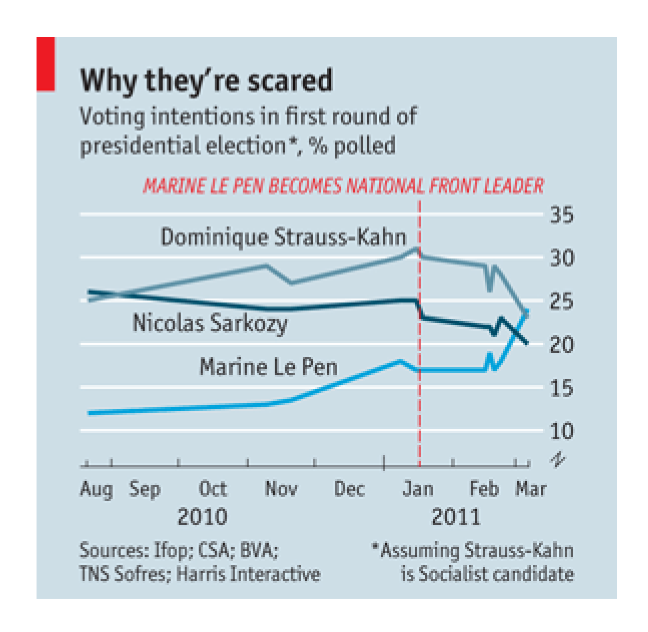
France's far right

They can't keep her down

What can France's political establishment do about the rise of Marine Le Pen?



THE setting was as carefully chosen as her words. Marine Le Pen, the new leader of France's National Front, dropped in to visit an immigrant-detention centre on the Italian island of Lampedusa this week, to alert the French to the "waves of immigration" flooding in from the Arab world. But she mixed hard talk with a disarming air of compassion. "If I listened only to my heart, of course I would let you board my boat," she declared. "But my boat is too fragile and, if I take you, my boat will sink...Europe does not have the capacity to welcome all these illegals." The moment captured all that makes Ms Le Pen such a threat: an eye for a stunt, an appeal to populist fears, and above all a knack for dressing up intolerance as common sense.



A year before France's presidential election, the woman who only recently stepped out of the shadow of her father, Jean-Marie, is rocking the political establishment. Last week, when a poll showed that Ms Le Pen would beat President Nicolas Sarkozy into the second-round run-off, his aides tried to dismiss it as an outlier. But since then other polls have found the same. Ms Le Pen could squeeze out the unpopular Mr Sarkozy with support of just 19%, according to one poll. Her best first-round score so far is a hefty 24% (see chart).

Although voting is still a year away, these polls are exercising many French people for a simple reason: they have already lived through the shock of electing the National Front into the second round. In 2002 Jean-Marie Le Pen, a blustering former paratrooper, beat the Socialists' candidate, Lionel Jospin, into the run-off against Jacques Chirac. Ms Le Pen stands virtually no chance of winning in 2012. But she could cause trouble by pushing out one of the mainstream candidates in the first round, as her father did. And this time, both the left and the right are vulnerable.

Ms Le Pen's ascension is all the more remarkable given the nature of the National Front. She is a woman in a party with a strong macho current. She is divorced, in a far-right milieu with traditional Catholic overtones. She is young, at 42, in a movement that draws heavily on older voters. Yet this lawyer and member of the European Parliament seems to be

turning all this to her advantage, rejuvenating the Front and ridding it of the jackbooted imagery that clung to her father. Whereas Jean-Marie thundered about losing Algeria and dismissed the gas chambers as a "detail" of history, his daughter has called the Holocaust "the height of barbarity". With her courteous demeanour and tempered vocabulary, she is single-handedly decontaminating the National Front brand.

What Ms Le Pen shares with her father is an anti-establishment and anti-European appeal to ordinary folk turned off by the cronyism of the left and the right. In that she may be boosted by Saif al-Islam Qaddafi's claim this week that his father's regime helped finance Mr Sarkozy's election campaign. (The Elysee denied the claim, and Mr Qaddafi provided absolutely no evidence, though said he would.)

Ms Le Pen wants to withdraw France from the euro, and to re-erect border controls with neighbouring countries. Yet she has deftly recast her father's more toxic talk about immigration and Islam. Although she still wants to end all immigration, give French nationals preference for jobs and bring back the death penalty, out has gone the obnoxious xenophobic tone. Instead she casts herself as the defender of cherished French principles: *laicite* (secularism) and women's rights. When she compares Muslims who pray in French streets to the Nazi occupation, she says this is not a gesture against Islam but a secular effort to keep religion out of public space. Who, she seems to say, could disagree?

Fewer and fewer people, it appears. One poll this week, by TNS Sofres, found that 38% of respondents think of the National Front as a party of the patriotic, traditional right (rather than the extremist, xenophobic variety), up from 28% a few years ago. Mr Sarkozy has said his party will fire any candidate who tries to make a local electoral pact with the Front. Even so, in two-round elections in French cantons, on March 20th and 27th, the National Front could make it into the second round in up to 200 of the 2,000-odd constituencies, not only in the south, its traditional base, but in the old industrial towns of the north and rural districts, too. No longer just a party of protest, the Front is seeking to govern.

What can mainstream politicians do? In the past Mr Sarkozy reached out to far-right voters with coded talk about immigration, declaring that "if anybody doesn't like France, they should leave". In 2007 this ate into Mr Le Pen's vote, keeping him out of the run-off. In office, Mr Sarkozy has kept at it, creating a (short-lived) ministry of national identity, tightening immigration and citizenship laws, banning the burqa and closing Roma camps.

This approach seems to have reached its limits. Instead of robbing the far right of votes, Mr Sarkozy appears now to be handing them support. Take a plan for a "national debate" on *laicite* in France on April 5th. Just like yet another debate on "national identity" two years ago, it looks more like an electoral stunt than a serious effort to reflect on the place of Islam in France. His own voters sense opportunism. Muslims feel stigmatised. Mr Sarkozy's "diversity" adviser, Abderrahmane Dahmane, was fired last week after calling on Muslims not to renew their membership of the ruling party unless the debate was cancelled. Claude Gueant, the interior minister, had to go to the Paris Mosque this week to calm matters. Meanwhile the National Front is quietly reaping the benefit.

Mr Sarkozy is in a corner. If he avoids the subject, he leaves the door open for the National Front. If he keeps stirring it up, he does their work for them. As for the Socialists, who ought to be exploiting Mr Sarkozy's unpopularity, they look just as exposed and unprepared. In the past Francois Mitterrand, a Socialist president, relied on the National Front to split the right. But working-class voters are deserting today's bourgeois Socialist Party for the Front as much as they are Mr Sarkozy's party. And the Socialists do not yet have a nominee for 2012. There are at least four serious potential candidates for this autumn's primary, among them Dominique Strauss-Kahn, head of the IMF. This week he appeared in a fly-on-the-wall television documentary to say that he had made up his mind as to whether to run...but would not reveal his decision until July.

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The far right in northern Europe

On the march

Populist anti-immigration parties are performing strongly across northern Europe

FRANCE is not the only European country suffering a far-right surge. In an arc of countries spreading north-east from the Netherlands, populist parties are cutting a swathe through politics, appealing to electorates with various blends of nationalism, Euroscepticism (and euro-scepticism) and outright xenophobia.

The country to watch is Finland, where the True Finns have emerged from obscurity to have a shot at joining government after an election on April 17th. Surging poll ratings (see table) put them on a par with Finland's three main parties. "If the party gets enough seats", says Pasi Saukkonen, a political scientist at Helsinki University, "it would be quite difficult to exclude them from negotiations." Timo Soini, the party leader, who casts himself as a jovial everyman, is pitching for the premiership.

The nasty crew

Far-right parties in northern Europe

	Political status	Latest opinion poll, % support	Seats in parliament	Key issues
Sweden Democrats	Opposition	5.7	20 of 349	Immigration, crime, Islam
Danish People's Party	Supporting minority government	15.2	25 of 179	Immigration, Euroscepticism, traditional values
True Finns	Opposition	16.9	5 of 200	The EU and euro bail-outs, immigration
Freedom Party *(The Netherlands)*	Supporting minority government	17.6	24 of 150	Islam, anti-establishment, law and order

Sources: *The Economist*; Demoskop; Gallup; Taloustutkimus; Synovate

Finland's mainstream politicians have acknowledged the ascent of the True Finns. Mari Kiviniemi, prime minister and leader of the Centre Party, says she could work with the party. Her finance minister, Jyrki Katainen, leader of the conservative National Coalition Party, says Mr Soini could be prime minister.

The party has broadened its appeal from its rural base and is filching voters from all sides. It adopts an anti-immigrant pose, but its signature issue is hostility to the European Union and particularly the bail-outs of poorer southern members of the euro by fiscally prudent northerners. Its influence may already be visible in the hard line struck by the Finnish government in recent euro-zone negotiations.

Another Nordic party that can point to influence over government is the Danish People's Party (DF). Under its influence the minority centre-right coalition it has propped up for the past decade has turned Denmark's immigration regime into one of Europe's tightest. The DF's leader, Pia Kjaersgaard, is often voted Denmark's most powerful woman, ahead of the queen. Buoyed by the government's appointment last week of a new gung-ho immigration minister, the DF upped the ante by demanding the prohibition of purpose-built mosques and compulsory psalm-singing in schools. It hopes to do well in elections that must be held by November.

Their Swedish counterparts, the Sweden Democrats, enjoyed success at a general election last September, entering parliament for the first time (decked out in pastoral national costume). There was speculation that they might become an ally of government. But unlike their Danish brethren they have been shunned by other parties. Last week Erik Ullenhag, Sweden's integration minister, accused them of intolerance and Islamophobia. But their poll ratings are holding up.

In the Netherlands the anti-immigrant Freedom Party (PVV) and its leader, Geert Wilders, are still hot stuff, despite an unspectacular performance in recent provincial elections. Polls put the party second only to the Liberals, whose minority coalition with the Christian Democrats Mr Wilders has supported in parliament since last year, in a Denmark-style arrangement.

Some in the political establishment thought that bringing Mr Wilders into power would temper his appeal. That plan does not seem to be working. Mr Wilders paints himself as an anti-establishment figure, but he is well versed in playing the system, exploiting his insider-outsider position to maximum advantage. His criticism of ministers can be scathing, but is limited to personalities, or issues outside the government agreement he has signed.

The PVV still plays the Muslim card-anti-Islamism, Mr Wilders says, remains his "passion"-but it is seeking to broaden its hand with other themes, ranging from the eccentric (expelling "imported" animal species such as Highland cows) to the worrying ("scum camps" for repeat offenders).

Other countries have not been immune to the far right's rise. Since 2009 the British National Party has been represented in the European Parliament. The Vlaams Belang remains a force in Belgium's dysfunctional politics. The virus, it seems, is spreading.

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Russia's regional elections

Attack of the clones

There are few surprises as the Kremlin's parties mop up the votes

ELECTIONS in Russia have long ceased to be a contest for power or a competition between ideas. Instead they play the role of a plebiscite for the Kremlin and United Russia-a special-purpose vehicle designed by Russia's rulers to ensure that they stay in power.

With the exception of the toothless Communists, all the parties in the Duma are integral parts of the political system set up by the Kremlin. Elections, like much of politics in Russia, are an imitation of the real thing. But the regional polls on March 13th deserve some attention, not least because they are seen as a dress rehearsal for a parliamentary vote in December and a presidential election the following March.

The general outcome was no surprise. United Russia, which has the entire Russian bureaucracy at its disposal, grabbed 70% of all seats in the 12 legislatures that held elections. Yet in terms of votes, the party did worse than in the previous parliamentary election, in 2007. It won over half the votes in only three regions. In the economically depressed region of Kirov, it received little over one-third.

On a turnout of less than 50%, this means that only a quarter of Russian voters plumped for the Kremlin's party. The rest either ignored the elections or voted against United Russia. The Communist Party came second with 20% of the votes, which gave them 13% of the seats. But liberal parties did not benefit. In the few regions where they were able to register, they won no more than 2% support.

The main surprise was the performance of a party that few had heard of. Patriots of Russia was set up six years ago, its website says, though it has since been largely dormant. Some of its candidates were apparently registered shortly before the polling date. Yet it managed to win nearly 8% of the vote. In Dagestan, in the troubled north Caucasus, it overtook the Communists.

Analysts say the party is another Kremlin product, tested now with a view to being deployed in the parliamentary election in December. It describes itself as a party of "statists" and "patriots" that aims to build a "great and prosperous" Russia. But its real purpose, it seems, is to act as a spoiler for the Communist Party and another party, Just Russia, which itself was originally created as a double for United Russia but has since become a genuine challenger.

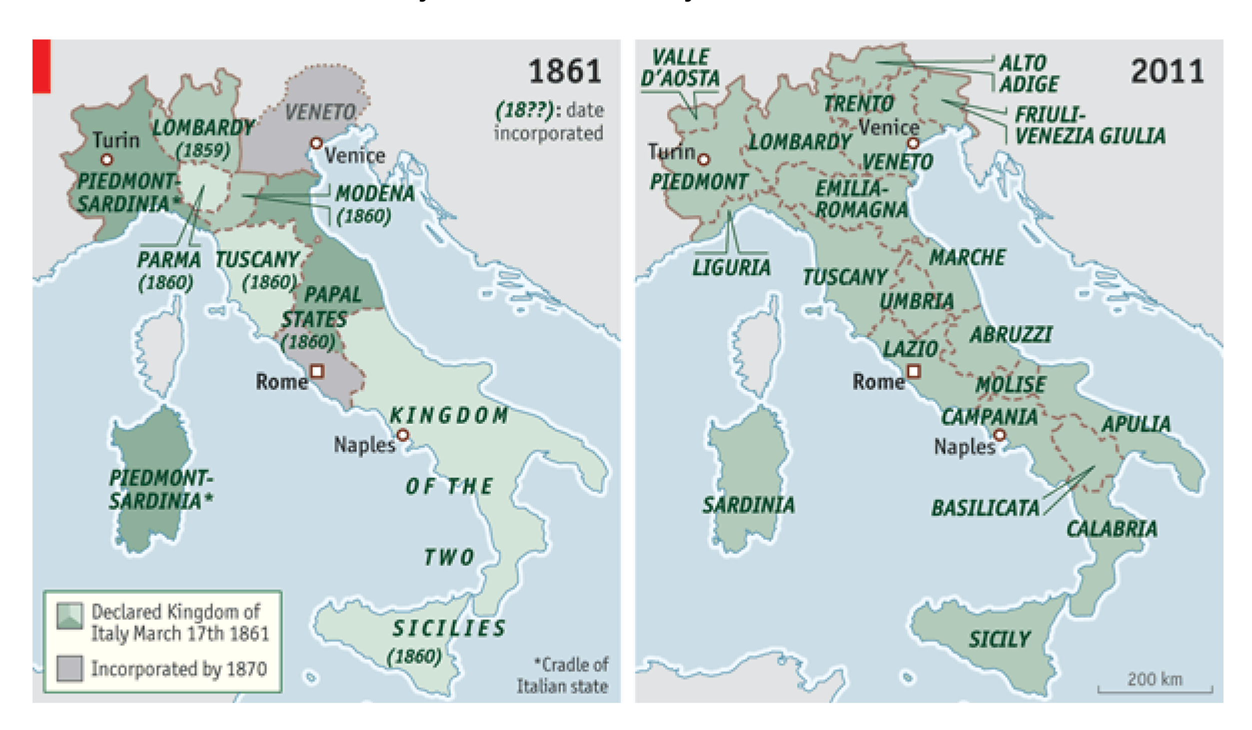
Engineering clone and fake opposition parties is one of the Kremlin's favourite political "technologies". But in its attempts to keep a lid on Russian politics, it likes to maintain parties of all shades and sizes. Patriots of Russia seems to be version two of Rodina (Motherland), a nationalist party set up before parliamentary elections in 2004 to take votes from the Communists and to whip up anti-Western rhetoric. Having performed this function, Rodina quietly disappeared, and its leader was rewarded with the job of ambassador to NATO. Patriots of Russia is likely to do a similar job in December's elections. Ostensibly it will be running independently, but actually it is designed to absorb and deflect Russians' growing nationalism, and their discontent with the Kremlin.

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Italy at 150

Happy-ish birthday

Italians feel ambivalent about their country's unification, 150 years on



ITALY'S military aerobatics team used vapour trails to trace what was claimed to be the world's biggest *tricolore*. Dignitaries converged on a ceremony at the capital's Altar of the Fatherland. And 3m Italians, according to a poll, planned to start a long weekend on the public holiday that marked their country's 150th birthday on March 17th. On that day in 1861 King Victor Emmanuel proclaimed the foundation of the kingdom of Italy.

Not everyone was celebrating. On orders from their leader, Umberto Bossi, officials of the Northern League worked as normal. The party's parliamentarians in Lombardy refused to sing the national anthem. Earlier this month in Vicenza some 200 people, reportedly including elected representatives of the League, burned in effigy the military hero of Italy's unification, Giuseppe Garibaldi.

The nominally separatist League props up Silvio Berlusconi's conservative government. So the prime minister approached the anniversary with trepidation. It was not until last month that his cabinet agreed that it should be a holiday.

Ironically, Mr Berlusconi can take some credit for helping unify Italy. His television channels challenged state broadcasters with lowbrow programmes in the Italian language that appealed to those groups most likely to speak regional dialects. In the early 1980s, when Mr Berlusconi's channels were starting up, fewer than 30% of Italians spoke only their national language. By 2000, 44% did. Still, it is striking how many Italians continue to speak dialect 150 years after the creation of their state.

Italy breaks the rule that young countries are uniformly patriotic. Italians may cheer for *gli azzurri* when their football side takes the field. Yet Mr Bossi's followers are not alone in feeling lukewarm about unification. Some southern intellectuals dispute the view that the overthrow of the Kingdom of Naples brought progress to a benighted Mezzogiorno.

After unification Massimo D'Azeglio, a Piedmontese statesman, remarked that, having made Italy, "we have to make Italians". But there was perhaps a more important objective: to reduce the vast economic differences between them. That task remains. Relative poverty in the south still fires the indignation of southerners and the exasperation of northerners alleviating it with their taxes. Launching the latest southern revisionist tract in Naples this week, one of its authors said that so long as the south has a GDP per head 70% of the north, "you can't talk about a united Italy."

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Tax torment

By picking on Ireland, the euro zone shows a worrying side to its "economic government"



POOR Enda Kenny. Folksy and ruddy-cheeked, the new boy from Dublin was roughed up badly by European leaders during his first outing to Brussels. The Irish prime minister caught the eye of the class bully, Nicolas Sarkozy. Nobody defended the taoiseach; even the head prefect, Angela Merkel, put the boot in.

Mr Kenny's offence? To seek help for his bankrupt country and to keep the promise he made to his voters to defend Ireland's low-tax system. At a summit of euro-zone leaders on March 11th-12th, called to launch the "pact for the euro" (a pledge to align members' economic policies and enhance their competitiveness, see article), his plea for a cut in the interest rate Ireland pays for its EU loans irritated Mrs Merkel; the bail-out terms were agreed on just three months ago. His defence of Ireland's 12.5% corporate-tax rate annoyed Mr Sarkozy, who regards it as "fiscal dumping".

The Irish financial crisis has many causes, but low corporate tax was not one of them. Attracting foreign investment offers Ireland its best chance of economic recovery and of repaying its debts-a fact recognised by the euro zone when it granted the bail-out. In any case, nominal corporate-tax rates hide a complex reality. Companies in France, with a rate double that of Ireland, enjoy so many exemptions and incentives that they end up paying substantially less tax than those in Ireland. At the summit the euro zone belatedly recognised that the interest rate it charges bailed-out countries (about 3% above the cost of raising the loans in the market) sinks troubled economies further into debt.

But there is no appealing to reason. The deal was clear: to secure lower interest charges, Ireland had to back down on tax. "We weren't very pleased with what the Irish had to offer," declared Mrs Merkel. Gallingly for Mr Kenny, who dared to challenge the honour code and lost, George Papandreou, his Greek counterpart, won a 1 percentage point reduction in the interest rate his indebted country must pay-apparently a reward for agreeing to an ambitious privatisation plan he had approved a month ago.

All this betrays Mr Kenny's inexperience. He knew he would come under pressure on taxes, but brought no alternative offering to satisfy Mrs Merkel (if not Mr Sarkozy). Herman Van Rompuy, the president of the European Council (who presides over the summits), suggested Ireland should sign up to a promise of "constructive engagement on tax co-ordination" on the basis of the pact for the euro. This meaningless commitment was intended to offer Mr Kenny an escape route. Instead he saw it as a trap. As positions harden, it is unlikely such an offer will be renewed when leaders meet at the next summit on March 24th.

Still, for all of Mr Kenny's mistakes, the beating he received reveals something disturbing about the nature of the euro zone's "economic government", as Mr Sarkozy likes to call the process of economic integration, complete with now-regular summits of the euro-zone states (plus countries that wish to join the pact). The euro zone talks of competitiveness, but seeks to deny Ireland its competitive advantage. It thus gives the impression of disliking internal competition, treating low taxes to attract foreign companies as an evil to be exorcised, not a virtue to be emulated.

Such *dirigiste* instincts raise legitimate worries about what should be a good idea in European tax policy: this week's proposal by the European Commission to create a simplified EU-wide system of calculating and collecting corporate taxes. This is not a harmonisation of tax rates, which will remain a national prerogative, but creates an alternative tax base to enhance the single market. The Common Consolidated Corporate Tax Base (CCCTB) would allow companies trading across the EU to set off losses in one country against profits in another. Tax would be collected by a single national authority and redistributed to treasuries according to a formula based on the group's assets, labour force and sales. It is designed to lessen the burden of filing up to 27 tax returns. It is also meant to reduce disputes over "transfer pricing", the means by which subsidiaries of a group seek to shift profits to where they will be taxed most favourably.

Crucially, the system would be voluntary. Each company would decide whether it wants to adopt the Europe-wide system or stick with national tax regimes. It should be most appealing to small and medium-sized companies seeking to expand beyond national boundaries, and to foreign firms that want to invest in Europe. European businesses have welcomed the proposal, as has the American Chamber of Commerce to the EU. Even a country such as Britain, which jealously guards its sovereignty on tax matters, thinks the arrangement might offer benefits.

But there are two political obstacles. One is the distribution of winners and losers in any new system of sharing out revenues. A second is the fear that a common corporate-tax base will be the first step to a common tax rate. A liberalising measure risks being turned into a protectionist tool. Given the antics of Mr Sarkozy and Mrs Merkel, can anyone blame Mr Kenny for declaring that the CCCTB is the "back door" to tax harmonisation?

Punch or parry?

Mr Kenny should fight for Ireland's right to set its own tax policies. But not every change need be an assault on Irish independence. With his country in such a weak economic state, Mr Kenny cannot risk a bare-fisted fight with his tormentors, however much the press may want it. Instead he needs to outsmart them.

So at the next summit in Brussels, he should declare that, in return for a cut in Ireland's interest rate, he will support the CCCTB, and challenge others to do likewise. Done properly, the plan would spur tax competition in Europe, particularly in favour of burgeoning firms, by making it clearer who offers the best tax rates. In an open and fair contest, the bullies may well decline to take on Mr Kenny. Many others will cheer him on.

Economist.com/blogs/charlemagne

The inscrutable chancellor

The Osborne identity

As he prepares for his second budget, the chancellor of the exchequer remains a mystery to many in Westminster



NO OTHER office of state carries the mystique of chancellor of the exchequer, a job that comes with almost prime-ministerial power but only a rare duty to enter the spotlight. The next of these occasions comes on March 23rd, when George Osborne delivers his second budget. Coalition government has left him even less visible, and less understood, than he might have been: Nick Clegg, the Liberal Democrat deputy prime minister, has become the second face of the coalition, alongside David Cameron, the prime minister.

Mr Osborne's elusiveness would matter less, were the gap between his public profile and his influence smaller. His plan virtually to eliminate the structural deficit in this parliament is the government's main task; the parallel project to reform the public services takes place within budgetary limits set by him. But his sway extends beyond the Treasury, where his seriousness and technical command have surprised civil servants who expected the neophyte of popular pre-general election caricature. Mr Osborne also does much of the government's political thinking. He is often the dominant voice in the kind of strategy meetings-many of which Mr Cameron lets him chair-in which he first shone as a young adviser in the 1990s.

He had few allies in the Conservative Party in opposition, but a support base is now growing under him. His special advisers are the best in the government. There are "Osbornite" MPs, such as Matthew Hancock and Greg Hands. His stock has risen on his party's right: many who once mistrusted his desire to move the Tories to the centre ground now see him as a more vigilant guardian of Tory views in the coalition than Mr Cameron.

None of this means that Mr Osborne is the "real" prime minister, as some maintain. Mr Cameron's decisions ultimately carry the day. Neither is their relationship anything like as fraught as that between Tony Blair and Gordon Brown. Mr Osborne is ambitious but knows that any opportunity to lead his party or country is years away. He also knows that, as our pre-budget opinion poll demonstrates (see article), voters are yet to warm to him.

Still, grasping the differences between the two men is crucial to understanding how the government works. The contrast between Mr Osborne, a lifelong metropolitan, and Mr Cameron, a son of the rural home counties, is often said to lie in the former's social liberalism. But Mr Osborne is more liberal on moral issues such as abortion and gay rights than on law and order. And on foreign policy, Mr Cameron would get an easier ride at a trendy London dinner party than hawkish Mr Osborne.

The real difference between them lies in their approach to politics. Mr Osborne is obsessed with winning. He is less moved by abstract ideas such as the "Big Society". He is more inclined to belligerence towards political opponents, whether they be trade unions or the Labour Party. Some Tories think they would now be governing alone had Mr Osborne run last year's election campaign by himself.

This hunger for victory comes from tasting multiple defeats as an adviser. Mr Cameron at least worked on the Tories' triumphant 1992 election campaign (Mr Osborne was still a student) and took a sojourn in business during the party's dog days later in the 1990s (Mr Osborne never left Westminster). The chancellor clocked that the Tories needed to soften their right-wing image long before Mr Cameron did.

In his economics, however, Mr Osborne is an old-fashioned Conservative. His free-market instincts sometimes show; he once flirted with the idea of a "flat", rather than progressive, income tax. He has been restrained in punishing the banking sector for its part in the financial crisis.

But, when it comes to the public finances, Mr Osborne is a sober fiscal hawk rather than a gung-ho Reaganite tax-cutter. Perhaps his best judgment came in opposition, in the period before the financial crash, when he resisted calls from the right to promise an overall tax cut. The subsequent crisis vindicated him, but Britain's relapse into negative growth in the last quarter has brought new demands for tax cuts, or, from the left, slower spending cuts. Voters are worried, as our poll shows.

Committed as he is to austerity, in his budget Mr Osborne is likelier to reform taxes than to cut them. That commitment is a political as well as an economic gamble: a double-dip, or even prolonged slow growth, would wound him. The economy will determine whether his credibility keeps soaring, or has already peaked.

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Anglo-American-Israeli diplomacy

All the president's messengers

Unravelling the riddle of David Cameron's views on Israel

AMONG even sharp-eyed observers of British foreign policy, the prime minister's views on Israel are a bit of a mystery. Squint, and there could almost be two David Camerons. The explanation might lie in the complex triangular choreography of Anglo-American-Israeli diplomacy.

First, there is Mr Cameron the typically "European" leader, pushing for Israel to offer concessions to the Palestinians and playing up his differences with America, Israel's main ally. This critical stance was on view during Mr Cameron's visit to Turkey in July 2010, when he compared the blockaded Gaza Strip to a "prison camp" and denounced the Israeli boarding of a flotilla of activists bound for Gaza. Last month, on a tour of Gulf states, this Mr Cameron went out of his way to highlight Britain's vote, a few days earlier, for a United Nations Security Council resolution condemning Israeli settlement activity-a resolution that America eventually vetoed. Mr Cameron told a group of Qatari students that, on this subject, Britain disagreed with its American ally.

The other Mr Cameron is Israel's loyal friend. That version was on display on March 2nd, when the prime minister spoke to the Community Security Trust, a British Jewish group. He said his "belief in Israel" was "indestructible"; discussing Israel's security needs, Mr Cameron veered away from the European consensus towards the sort of robust view more typically heard in Washington, DC. He said Israel was "within its rights to search vessels bringing cargo into Gaza".

Is this a case of a prime minister telling each audience what it wants to hear-and perhaps attempting once again to position his country as a bridge straddling the transatlantic policy gulf? Not entirely, at least according to one (contested) version of recent diplomatic history.

If Mr Cameron offers Israel mixed messages, he does so with the blessing of America's president, normally reliable diplomatic sources claim. Faced with what they see as the intransigence of the Israeli government led by Binyamin Netanyahu, Europe's big beasts and America are moving closer in outlook, according to those sources. Before the UN vote of February 18th, Barack Obama reportedly encouraged Mr Cameron and others to take a tough line on Israel. In phone calls to his European allies, Mr Obama is said to have expressed frustration at Mr Netanyahu's approach to settlements, but to have explained he had "too many domestic fires to extinguish" to risk a bust-up over Israel.

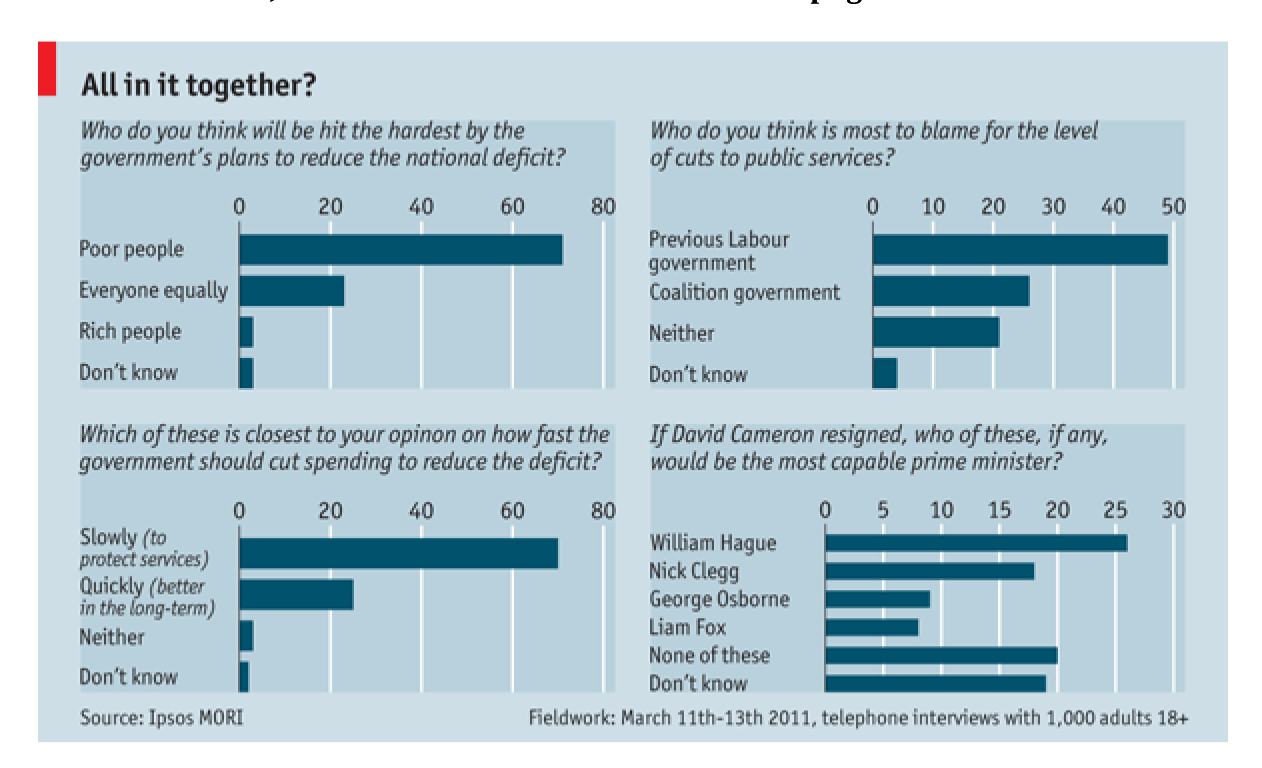
The White House strenuously denies this account. Number 10 would only confirm that Mr Cameron and Mr Obama had been in "regular touch" over the peace process. Since these are private conversations, it is tough for *The Economist* to know exactly what was said. But, in private, European officials have told Israel that their pressure is choreographed with America.

This, rather than hypocrisy, might be the real story of Israel's current relations with Britain and others. Impatience with Mr Netanyahu seems to be blurring the boundaries between Israel's friends and critics. And Mr Cameron's seeming disagreement with Mr Obama might actually be a form of diplomatic co-operation.

Our pre-budget opinion poll

More haste, fewer votes

The public doesn't like the cuts, but blames Labour for Britain's fiscal plight



THERE is bad news for the coalition in a poll commissioned by *The Economist* ahead of the budget on March 23rd. Many voters are sceptical about the government's approach to cutting the deficit. The better news is that quite a lot of them blame the previous Labour administration for the fiscal woe.

Ipsos MORI found that only 28% of the public thought the government has got the balance between spending cuts and tax rises right; 43% thought it is cutting too sharply and 20% that it is raising taxes too much. Meanwhile 70% said the cuts should be made more slowly to protect the economy, broadly the same proportion as when the question was posed last year. Ministerial rhetoric about Britons being "all in it together" doesn't wash: just 23% said deficit reduction would hit everyone equally; 71% thought the poor will fare worst.

Still, if the Labour opposition seems to be winning the argument about the pace and complexion of the retrenchment, it is losing the long-term blame game: the coalition's bid to attribute the pain to Labour's fiscal incontinence seems to have paid off. Given a choice between the coalition and Labour, 26% of the public thought the current government was mostly to blame for the level of cuts to public services; 49% fingered the previous one. When some respondents were offered a broader range of culprits, 29% plumped for "banks" and 18% "the state of the global economy"-but Labour was still chosen by 31%.

Another silver lining for George Osborne and the Conservatives, at least, is that voters feel less betrayed by them than by their Liberal Democrat partners: 44% thought the Tories have been truer to the plans for the deficit they announced before the general election; only 8% said the Lib Dems had been straighter.

But the picture is rather less rosy for Mr Osborne's personal ambitions. If David Cameron were to fall under the proverbial bus, 26% wanted William Hague to replace him, despite criticisms of the foreign secretary's recent performance. Nick Clegg, the embattled leader of the Lib Dems and deputy prime minister, was chosen by 18%. Only 9% went for Mr Osborne, one point more than Liam Fox, the Tory defence secretary.

For more polling results and charts, visit Economist.com/britain

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Libel-law reform

The price of truth

An overdue bid to protect free speech and deter frivolous libel claims



LITIGATION is a rich man's game. That will remain true even if the reforms to English libel law outlined by the government on March 15th come into force next year, as enthusiasts for an overhaul hope. But the proposed changes and clarifications might tilt the scales of truth against the litigious wealthy a little.

The biggest change is designed to restrict "libel tourism": lawsuits between foreigners fought in English courts. The use of London courts to sue Americans for material mainly published and read across the Atlantic has caused outrage among free-speech defenders in Congress and elsewhere; a proposed American law would allow defendants to counter-sue for harassment if they lose in a foreign case. Few such cases actually come to court, but when they do, they reek of unfairness: an English-language paper in Kiev, for example, now blocks British internet users from its website, to avert another costly libel action brought by one of the touchy Ukrainian tycoons who have used English courts to settle scores with the local media.

Another Ukrainian case suggested that judges have been wising up to tourism: last month a High Court judge struck out a suit against the same Kiev weekly brought by Dmitry Firtash, a Ukrainian oligarch; called his links to Britain "tenuous in the extreme"; and ordered him to pay the defendant's costs. The new draft law would create a proper legal barrier. Plaintiffs from outside the European Union would have to show that the bulk of the damage to their reputation occurred in England or Wales (Scotland has its own courts): tough if you live in Dniepropetrovsk. All plaintiffs will have to demonstrate "substantial harm" to their reputations.

Among other changes are curbs on (rare) jury trials in libel cases. These are expensive and slow; if a plaintiff's lawyer demands one, defendants can be intimidated. Some old barnacles will be removed from the legal system. It will no longer be slanderous to impute unchastity to a woman, or to say someone suffers from "venereal disease, leprosy or the plague".

More important are the proposed new statutory defences against libel claims: truth, public interest and honest opinion. These are meant to replace the existing thicket of judge-made law from past cases, such as the "Reynolds defence", which sets out, in a complicated and much-contested way, what a good journalist ought to do before publishing a controversial story. Reports of public proceedings and conferences will gain some protection too.

Ken Clarke, the justice secretary, especially wants to stop attempts to "stifle" scientific debate. Academics and journalists feel strongly about this. An article describing chiropractors as "bogus" prompted a lengthy, expensive (and ultimately fruitless) suit from their trade body. Some mainstream medical outfits are sensitive too: an American firm, NMT Medical, is suing a cardiologist, Peter Wilmshurst, for publicising a medical trial that suggested its device did not work. The process has cost him pound100,000 so far.

Campaigners for reform welcomed the plan, which draws on work by Lord Lester, a Liberal Democrat peer. In the consultation period until June they will lobby for curbs on companies' rights to sue and stronger protection for online publishers.

But some gripes remain. For instance, the new code in part simply relabels existing defences. The actual difference between the old "fair comment" defence and the new one of "honest opinion" might itself be a subject of lengthy and lucrative debate. Using words such as "corrupt" will still be riskier in England than in America, where claimants must prove that journalists were malicious, not just hurtful.

Costs will remain high too, at least until judges have a chance to chew on the meaning of the new terms. Reformers should be "careful what they wish for" says Rod Christie-Miller of Schillings, a particularly ferocious firm of London libel lawyers: "The more laws you make, the more money lawyers make." The most effective reform would encourage plaintiffs and defendants to settle cheaply and out of court. That is yet to come.

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Public-sector pay

The cap doesn't fit

Advice for the government on a sensitive remuneration issue



Hutton's way

THE justice of public-sector pay is a neuralgic issue at the best of times-which these are not. Keen to show concern for the complaints of the low-paid, but mindful of the potential for stoking unrest, last year the government set up a review of pay differentials in the public sector-but farmed out the task to Will Hutton, boss of the Work Foundation, a think-tank. Mr Hutton is also a left-leaning columnist, and thus not a typical state-slashing free-marketeer. He produced an interesting but perhaps not definitive report on March 16th.

He was charged with finding ways to make public-sector pay "fairer", and implicitly with addressing the sporadic eruptions of concern over public-sector "fat cats". His report attempts to outline a way of ensuring that the bosses are paid well enough to attract and retain the best, but not so well as to invite allegations that the state is funding a costly gravy train.

What it didn't say was most striking. Mr Hutton eschewed an idea he had floated earlier, of creating a link between top managers' pay and the lowest pay of their staff. A mooted maximum salary ratio of 20:1 is, he now says, unworkable. It would also be vastly unpopular among the best-paid public servants and at odds with Mr Hutton's other declared objective of attracting talent to the public services.

Instead he proposes an "earn back" scheme for around 20,000 senior staff, which would link a proportion of their basic pay to agreed performance targets. Those who failed to meet them would lose it; those who exceeded the targets would qualify for bonuses. "No pay system can be fair if it fails to reflect individual performance," he concludes; the public sector needs to spell out its view of success and failure and distribute rewards accordingly.

The problem lies in creating a solution less flawed and distrusted than private-sector bonuses, which are often divorced from tangible proof of rising performance. In assessing the value of a senior health-service manager or council chief, for example, the line between core competence and bonus-worthy brilliance might be hard to define. University vice-chancellors-in whose remuneration the government has an indirect say-might be judged largely by their success in attracting able students from poorer backgrounds (a goal of government policy). However laudable that aim, using it to determine vice-chancellors' pay might distort admissions decisions.

Previous administrations have struggled with this issue. The Labour government's bid to introduce performance-related pay for teachers ended up with the supposed incentive turning into a hidden general pay rise. Its efforts to motivate GPs by giving them new contracts in 2004 failed to secure a conspicuously better deal for their patients.

Mr Hutton proposes a system of non-executive governance to keep the self-regard of bureaucrats in check, and the appointment of a representative employee to new remuneration committees. That idea produced scepticism in government about the virtue of creating another layer of oversight. But Mr Hutton makes a sensible point about transparency. He recommends that the pay of those at the top of the public-sector should be openly compared with the median levels of pay earned by staff in their services. This, he thinks, will result in downward pressure.

A veteran of the New Labour years, Mr Hutton evidently believes targets are the key to accountable public services. Yet the coalition has in general derided Labour's inclination to meddle from the centre. George Osborne, the chancellor of the exchequer, now has to decide whether to accept the spread of bonus culture throughout the public sector-or shelve Mr Hutton's review and think again.

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Britain's new Olympic sports

New balls, please

The host nation extends its sporting repertoire



Handball, not a hand-ball

WHEN you have a children's party at your house, you get to choose which games the little guests may play. If you host the Olympics, the International Olympic Committee (IOC), not you, lays down the law. There will be 26 sports at the games in London next year, for which tickets went on sale on March 15th.

Manners dictate that places be reserved for the host country's athletes, in case they do not qualify for the games on their own merits. In some sports, they might not. Britain has a thin record in several Olympic disciplines. No British handball or volleyball team has ever taken part, save a female beach-volleyball pair in Atlanta in 1996. A men's basketball team has played once-in 1948, the last time London was host.

The host country does not have to take part in everything, but British athletes are undaunted. The British Olympic Association (BOA) has said that to earn a slot, a team must be capable of "a credible performance". A sport must leave a "legacy", encouraging more people to play and coach. It approved volleyball in December and handball in January. In

basketball, the one sport in which the BOA does not have the final say, FIBA, the global governing body, said on March 13th that British teams could play.

Of the new sports, hopes are probably highest for basketball, which is also the best financed. Two of the men's squad play in the National Basketball Association in America, by far the world's leading league; most of the rest play in continental Europe. Both the men's and women's teams have made it to the European championships this year. Chris Spice, British Basketball's performance director, says the aim is to qualify on merit for the 2016 games in Rio de Janeiro.

The handballers and volleyballers are improving too, but have farther to go. The men's handball team (in action in the picture) won its first competitive match only last year, against Bulgaria. In volleyball Britain's men are ranked 94th in the world, below the Maldives. The women are 72nd, below Belize. In other countries both sports are big enough to support professional leagues; in Britain, neither is. British handballers are playing in Germany, which has Europe's best league, and elsewhere to improve their game.

Female volleyballers are playing in Europe too, getting by on as little as euro500 a month: unlike the men, they receive no public money. Lynne Beattie, the captain, says she is "in a worse state financially than when I was a full-time pharmacy student." The team has "a constant struggle just to make ends meet." But marginal sports' officials must eke out their funds, because UK Sport, which distributes public money, puts most cash where prospects are brightest.

Might the Brits fare better if the IOC let the hosts choose the sports? Maybe. Britons aren't bad at golf and rugby, which will be played in Rio but not in London. Or maybe not. Given England's displays in the current World Cup, it might be just as well that there's no Olympic cricket.

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Bagehot

The Lib Dems wobble

It is much too soon for David Cameron's coalition allies to lose their nerve



SHORTLY after the general election of 2010, a Liberal Democrat adviser drew the party's MPs a chart of political imperatives for the next five years. The (unstated) aim was to show them how to avoid the traditional fate of Liberals entering a British coalition, namely, annihilation.

Richard Reeves-now an aide to Nick Clegg, the party leader and deputy prime minister-sketched three lines on a graph. One represented "Impact", or the ability to affect coalition policy. It was flat, showing a constant level of importance. One was marked "Credibility", representing the Lib Dems' claim to be a serious party of government, taking tough decisions (and showing Britons that coalition rule need not resemble stoats fighting in a sack). This line started high and slowly declined as a priority. That represented a hope: that voters would forget they once thought of the Lib Dems as a fringe party of hairy lentil-eaters and would grow used to Lib Dem ministers striding about deciding things.

The third line was marked "Identity" and represented a promise: that after a while, Lib Dems would be unleashed to boast about all the nice, liberal things they had achieved in office. This third line only emerged after some time, but rose to become all-important by the presumed election day in 2015.

There is no guarantee that Mr Reeves's pocket map will lead Britain's third party to safety. But it is an excellent guide to what is going on inside the Lib Dems, as David Cameron's coalition partners endure their bumpiest weeks since entering government. After not even a year in power, many Lib Dems are weary of building up credibility, and desperate to reassert their identity.

Mr Clegg has duly started flirting with what his team calls "positive differentiation". At a spring party conference in Sheffield on March 12th and 13th, he claimed credit for kindly things that a "government without Liberal Democrats" would not have done, such as tax cuts for the lowest paid. He declared the Lib Dems a party not for "the wealthy", but for early-rising strivers he collectively dubbed "Alarm Clock Britain" (a straight lift, by the way, from a campaign slogan of the French president Nicolas Sarkozy, who wooed "the France that gets up early").

Many party bigwigs are delighted by these signs of independent life. Tim Farron, the party's president and an ambitious MP on its left, enthuses that Sheffield demonstrated "purpose and spikiness and difference". A senior MP and Clegg ally on the free-market "Orange Book" wing says it is vital to avoid looking like a "shambolic", warring coalition, but also that it is "important to show we've made this a more compassionate government."

A minority fears it is too soon for identity politics. Julian Astle, director of CentreForum, a liberal think-tank, worries about a premature "loss of nerve", as the party is buffeted by headlines that will be largely forgotten in four years' time. The coalition with the Conservatives is still new, and "its stability should not be taken for granted", he says.

The problem is that Lib Dems are not enjoying life much. Mr Clegg has been burned in effigy by students, after breaking a pre-election pledge to oppose a rise in university-tuition fees. There have been grim by-election results, including a jaw-dropping sixth place in Barnsley Central (where the Lib Dem candidate was spat at in the street). A revered party elder, Lady Williams of Crosby, branded as "lousy" government proposals to shake up the National Health Service, a view echoed at the Sheffield party conference, which demanded changes to the NHS plans. After losing the state funding given to opposition parties, the Lib Dems are hard-up, and leaving their stately Westminster HQ. Polls put Lib Dem support at 10% nationally, and just half that in Scotland and Wales, where regional elections will be held on May 5th.

The same day will see a referendum on changing the electoral system for the House of Commons to the Alternative Vote (AV), in which candidates are ranked in order of preference. That system, which redistributes votes from eliminated candidates until someone crosses the 50% line, is marginally helpful to smaller parties, and very helpful for those, such as the Lib Dems, who might hope to form electoral pacts, as it allows supporters to give allies their second preferences. Alas, Mr Cameron is under pressure from his own party to campaign hard against AV, and-says a Tory MP involved in the "No" campaign-has sanctioned attacks portraying AV as a "vote for Nick Clegg", painting the Lib Dem boss as a would-be kingmaker in future elections.

A protest party grows up

So which path should the Lib Dems follow? They might not want to hear it, but, for now, their best hope remains credibility. Their identity is currently toxic. Voters who resent the rich do not think of Lib Dems as "compassionate", but as Tory stooges.

Some Lib Dem suffering is painfully ironic: they are attacked now as unprincipled rogues saying anything to get ahead. Actually, that is a good description of how Lib Dems used to behave: now they are firmly bound to painful cuts and other policies in their coalition agreement. Their party coasted on protest votes for years, latterly pretending to be some sort of left-wing conscience for Labour. That was never really accurate, and many left-leaning supporters are gone for good.

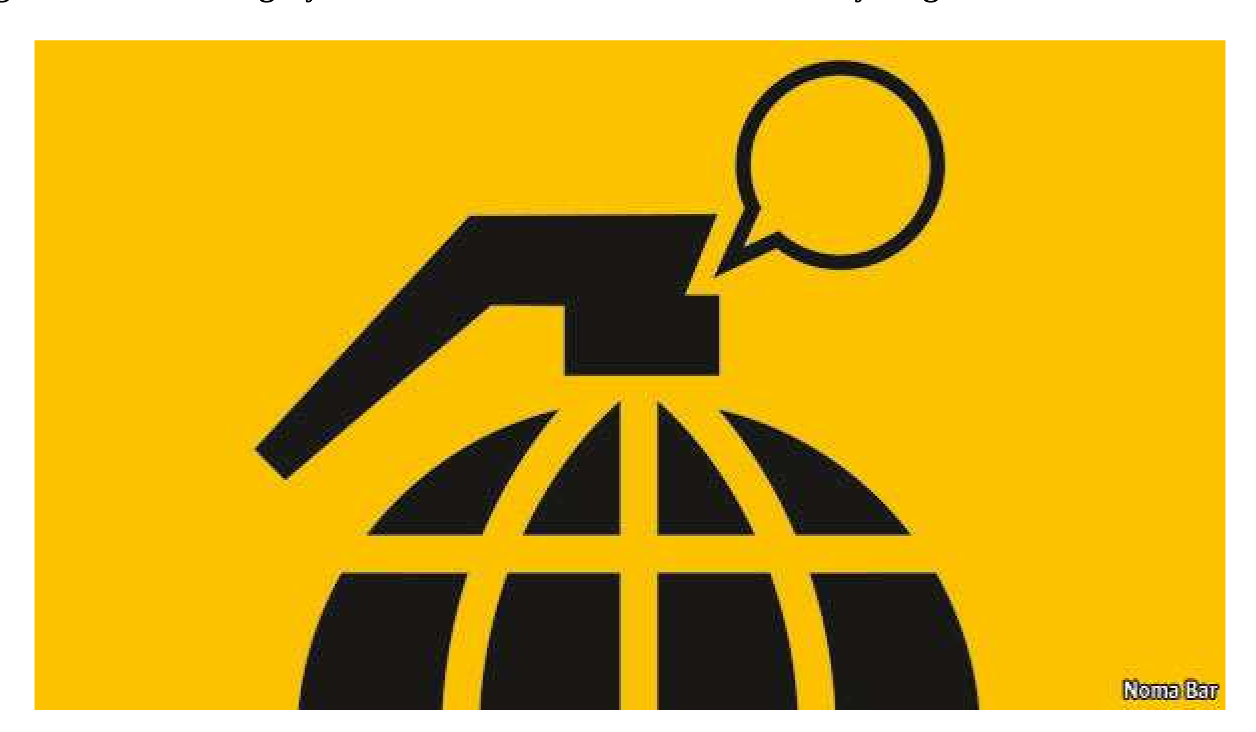
Are they doomed? A vote for the Lib Dems was once seen as wasted. That didn't trouble one camp of voters (who loved the purity of opposition). It put off a second camp (centrists who actually cared about how the country was run). Now that the Lib Dems are a party of government, the wasted-vote argument is weakened. If the second camp turns out to be bigger than the first, the Lib Dems might survive in 2015-providing, of course, that the coalition saves the economy in the meantime. Back to work, Lib Dems. This is no time for self-indulgence.

Economist.com/blogs/bagehot

Failed states

Where life is cheap and talk is loose

Modish jargon or a useful category? The term "failed state" conceals many tangles



THE annals of diplomacy recorded something startling in February. Saying, in effect, that it was in danger of collapse, the West African state of Guinea voluntarily turned to a United Nations agency that deals with failed or failing states. Like most of its neighbours Guinea has a history of violence, weak governance, poverty and destructive competition for natural resources. Its new government sought help from the UN Peacebuilding Commission, an unwieldy body that duly set up a task force known as a "country-specific configuration" to bolster the government in Conakry. It is already involved in shoring up half a dozen other countries, all African, at the behest of the Security Council; but this was the first time a country owned up to being at risk.

Such honesty is rare, but states that cannot control their territories, protect their citizens, enter or execute agreements with outsiders, or administer justice are a common and worsening phenomenon. Robert Gates, America's defence secretary, says "fractured or failing states" are "the main security challenge of our time." The term now extends beyond the poor world: American officials have applied it to the Italian region of Calabria.

The problem has attracted lots of wonkish experts, who have offered their expertise to the American government. As a scholar, Susan Rice used to berate the Bush administration for calling broken states a deadly threat but failing to fix them. Now she is her country's envoy to the UN. As a Princeton professor, Anne-Marie Slaughter was a leading academic authority on benighted places; till last month, she was a policy planner at the State Department.

This brainpower has yet to turn the tide of anarchy. In places where the state is chronically weak, it is not improving much. The spectre of state failure is haunting hitherto calm locations too. An annual ranking published by the Fund for Peace, a think-tank in Washington DC, always features the usual black spots: Somalia, Congo, Afghanistan, Haiti. Applying a fairly strict standard, it finds that most countries in the global South face some threat to their proper functioning.

Politics can complicate diagnosis and prescription. In a topical bit of scaremongering a Texas-based think-tank, Stratfor, has voiced fears that the drug-related mayhem engulfing parts of Mexico could end in state collapse. But the State Department would never bring that language to a delicate relationship. In some contexts, the use or non-use of words is a political choice. Last year, when Russia's President Dmitry Medvedev suggested that Kyrgyzstan was at risk of failing, he wasn't engaging in political analysis but hinting that Moscow's fatherly hand might again be needed to keep order.

Some semantic history may help. "Failed state" entered the political lexicon with the (ill-fated) American-led venture in Somalia in 1992. With cold-war patrons gone, so the theory went, many poor states were at risk of collapsing into Hobbesian anarchy, with dire results for their own inhabitants and neighbouring lands. Robert Kaplan, an American writer, captured and somewhat exaggerated an important truth by describing the chaos engulfing Liberia and Sierra Leone and warning of the "coming anarchy" in other parts of the world.

When words become deeds

No sooner was the term "state failure" born than political scientists began picking it apart. "Failure" may misleadingly imply that a government is trying to function but not managing. In fact, dysfunctional statehood may suit the powerful. As Ken Menkhaus of Davidson College in North Carolina has written*, the last thing a kleptocrat needs is good judges, or robust ministries that could be power bases for rival robber barons. "Where governments have become deeply complicit in criminal activities...perpetuation of state failure is essential for the criminal enterprise to operate."

Yet even fairly bad rulers, say African or Afghan warlords or corrupt provincial governors in Russia, may feel the need to provide certain public goods, if only to further their own interests. Such public services might range from half-decent roads to the suppression (or perhaps limitation through taxing) of petty crime. What those rulers will not do, though, is create an arena in which other economic or political players can emerge. Is that a success or a failure, then?

The English word "fail" can imply a status: a binary category into which you (or your exam paper) either fall or don't fall. Or it can be a process of indefinite duration. The second sense is more useful when discussing the welfare of states, where no bright line separates success and failure. Nor is there a continuum stretching from dismal failure to blessed success. The conditions are mixed in a variety of ways.

In the case of Mexico, it is hard to deny that governance is failing at some levels: some municipal police and councils, and authorities in certain states, have been infiltrated by the narco-mafia, becoming useless or worse in any fight against the drug trade. But the government can still marshal a formidable array of forces against the traffickers; that is quite a different situation from the anomie of Congo or Somalia.

Anarchy's anatomy

Failed states, 2010

Country *(Population, m)*	Failed states index, score*	Life expectancy, years	Symptoms
Somalia *(9.4)*	114.3	51.5	Anarchy, civil war, piracy
Chad *(11.5)*	113.3	50.0	Desertification, destitution, meddling neighbours
Sudan *(43.2)*	111.8	59.8	Ethnic, religious strife, illiteracy, tyranny
Zimbabwe *(12.6)*	110.2	50.4	Economic collapse, kleptocracy, oppression
Congo *(67.8)*	109.9	48.8	Civil war, massacres, mass rape, looting
Afghanistan *(29.1)*	109.3	45.5	Civil war, drugs, no infrastructure, terrorism
Iraq *(31.5)*	107.3	70.2	Ruined infrastructure, sectarian strife, terrorism
Central African Republic *(4.5)*	106.4	48.6	Desertification, destitution, disease, terrorism
Guinea *(10.3)*	105.0	60.1	Destitution, drugs, kleptocracy
Pakistan *(184.8)*	102.5	68.0	Coups, drugs, illiteracy, terrorism
Haiti *(10.2)*	101.6	62.1	Deforestation, destitution, crime
Côte d'Ivoire *(21.6)*	101.2	59.6	Incipient civil war, post-election deadlock

Sources: The Fund for Peace, *Foreign Policy*; UN; *The Economist* — *Out of a potential 120, based on 12 indicators

Calling Afghanistan a failed state seems less controversial, but in a land where central power has always been weak, what does success mean? The American-led coalition's goals include the defeat of the Taliban, the interdiction of the opium business and the bolstering and cleaning up of the government in Kabul. But such aims may be hard to reconcile, argues Jonathan Goodhand of London's School of Oriental and African Studies. The drug economy may have had a stabilising effect on some parts of Afghanistan, he has written; the only plausible hope of a functioning state may rest on a compromise among regional barons whose power rests on narcotics.

If this is even half-right, then success is hard to imagine, let alone achieve. And many an outsider has grown cynical about the prospects of even partial success in establishing a clean government in Kabul. Local support for clean governance is too weak; many hidden channels link the state, the drug lords and even the Taliban.

Another category of states, hard to place on any spectrum of success or failure, could be described as "brittle" dictatorships, like the communist regime that once ruled Albania or the one that still holds sway in North Korea. Such regimes are successful in the sense that they manage, as long as they last, to make people do what they are told; but once they fall, such polities can shatter into a thousand pieces.

Beyond good and evil

Nor is there anything simple or Manichean about the standoff between the state on the one hand and its would-be wreckers on the other. States that are fighting either terrorist or criminal groups often respond by sponsoring their own terrorist or criminal proteges. At that point it can be hard to make any moral distinction between pro- and anti-state forces.

Moreover, anti-state forces (such as the Tamil Tigers, the IRA in Northern Ireland, or the Kosovo Liberation Army) often function rather like states in the territory they control, operating welfare services and primitive justice systems, while at the same time engaging in crime, from organ-snatching to bank heists, to keep their coffers full. Such organisations may "go straight" when they gain a degree of formal political power. Or they may not.

Given the messy intractability of state failure, who or what has a chance of solving it? Coaxing states in the direction of success, so that relatively clean institutions drive out the dirtiest ones, may be the most realistic goal. But if dozens of the world's states are in some sense failed, and may well have a stake in covering up the failure of others, then help offered by yet more governments, or inter-governmental agencies, is unlikely to be a panacea.

To see the difficulties of what pundits call a "state-centric approach", consider the history of the UN Peacebuilding Commission. It was one of the big ideas to emerge from a reflection on the UN's future by the global great and good in 2005. As first conceived, it would have had enforcement powers and tried to pre-empt state failure, not just cure it. But many governments, jealously guarding the cloak of statehood, lobbied to keep the commission weak.

To have any hope of success, state-mending efforts must tackle benighted places as they really are, says James Cockayne, who co-directs a New York think-tank called the Centre on Global Counterterrorism Co-operation. They must cope with local power-brokers with no particular link to state capitals; and also with anti-state forces with global connections that could never be trumped by a single national government, even a clean one.

The clearest cases of such transnational state-spoilers concern the drug trade. As long as Latin American narco-lords find it easy to sell cocaine and buy guns in the United States, no government to the south can eliminate them. Whether in Latin America, in Afghanistan or in the emerging narco-states of West Africa, purely national attempts to deal with drugs can be counter-productive; they just drive up prices or create new networks.

In many other cases the wreckers are too effectively globalised for any one state to take them on, adds Mr Cockayne. Examples include Somali warlords with deep ties to the diaspora and Western passports; Congolese militia leaders who market the produce of tin and coltan mines to end-users in China and Malaysia; Tamil rebels who used emigre links to practise credit-card fraud in Britain; or Hezbollah's cigarette smuggling in the United States.

No worthy effort to train civil servants in just one capital will be of much use in neutralising these global networks. Last November the UN Security Council took a step towards recognising this. It passed a resolution telling buyers of tin not to source their raw material from mines controlled by Congolese militia leaders.

It was highly unusual for the council to issue an order to anybody except governments. Global Witness, an anti-corruption outfit, has reported that the resolution has been badly enforced, with only half-hearted efforts at self-policing by the tin

industry. But at least the UN may be edging away from the fiction that governments, and people under their orders, are the only factors that determine the fate of nations.

*Ending Wars, Consolidating Peace: Economic Perspectives, ed Berdal and Wennmann, IISS

A special report on the future of the state

Taming Leviathan

The state almost everywhere is big, inefficient and broke. It needn't be, says John Micklethwait

THE argument sounds familiar. The disruptive reforms that have so changed the private sector should now be let loose on the public sector. The relationship between government and civil society has been that between master and servant; instead, it should be a partnership, with the state creating the right environment for companies and charities to do more of its work. The conclusion: "We are in a transition from a big state to a small state, and from a small society to a big society."

A Republican presidential candidate in America? David Cameron rallying Britain's Tories? Neither: the speaker is supposedly China's most highly regarded bureaucrat. Last year Ma Hong won the country's national award for government innovation-a great coup for her department, which is trying to get more non-governmental organisations (NGOs) to take over parts of welfare, health and education services in the city of Shenzhen, just across the border from Hong Kong.

The award partly reflects the whirl of activity that is Ms Ma. She has dismantled most of the controls on local NGOs: rather than be sponsored by some government department, all they have to do is register with her. She began in 2004 with industrial associations, but has extended the net to include independent charities. Almost 4,000 "social groups" are now registered-nearly double the number in 2002, when they were all tied to the state.

Over the past five years Ms Ma has paid out 400m yuan ($57m) to the NGOs for social work, mainly to do with the elderly. The groups are evaluated by third parties on things like their corporate governance: the higher their rating, the more money she trusts them with. She provides training in social work and tax advice. She would like donations to more NGOs to be tax-deductible, as in the West.

Ms Ma has studied what works elsewhere. In Hong Kong, where she trained in 2005, some 90% of social work is done by NGOs, paid for by the state. Like many Chinese bureaucrats, she also admires Singapore-especially its balance between easy registration for NGOs and stern punishment if they underperform. She wants her social groups to become the engines of Chinese society "just as private companies are in the economy".

Even allowing for Ms Ma's dynamism, there was, as so often in China, a message implied in her award. The country's rulers are acutely aware that their government does not serve ordinary Chinese well. Back in 2007 the five-yearly Congress of the Communist Party embraced "scientific development" to create "a harmonious society". Shenzhen is supposed to be the showcase for a new public sector, just as it showed the rest of the country how to embrace capitalism 30 years ago. The city has classified some 280 government functions as "social" ones, which means they can be contracted out to Ms Ma's NGOs.

It is not hard to poke holes in China's version of the Big Society, as we shall see later in this special report. But there is plainly a drive to make government work a little more like the private sector. "Just as a human has two legs, China has a very long economic one and a very short social one," observes Ms Ma. "They should be of equal length."

Many Western politicians feel the same way about their own bloated and inefficient governments. The immediate problem is the financial crisis: governments have had to spend furiously, both to prop up their banks and ward off a depression. With the average gross debt burden in OECD countries just over 100% of GDP and sovereign-debt markets fearful of

another Greece or Ireland, every government, even America's, is under pressure to produce a credible plan to shrink its deficit.

What is government for?

Costly though it has been, the financial crisis has merely brought forward a fiscal reckoning. In most of the rich world ageing populations have been driving up the cost of public health care and state pensions. Emerging countries that are becoming richer, such as China and India, are now wondering what sort of state they need to meet their citizens' demands for better schools, health care and infrastructure.

Indeed, the fiery argument about capitalism prompted by the credit crunch has obscured a nascent, and much broader, debate about the nature of government. The future of the state is likely to dominate politics for the next decade at least. How can government be made more efficient? What should it do and not do? To whom should it answer? Ms Ma is one voice in this, but so are the anti-tax tea-party activists in America, French workers protesting against later retirement and British parents trying to set up independent schools with state money.

This special report's central argument is that Leviathan can be made far more efficient. The state has woefully lagged behind the private sector. Catching up is not just a case of nuts-and-bolts productivity improvements but of liberal principle: too often an institution that, at least in a democracy, was supposed to be the people's servant has become their master.

But nobody should expect that to be easy. The vested interests opposing change are huge: the state's growth has been encouraged by the right as well as the left, by favour-seeking companies as well as public-sector unions, by voters as well as bureaucrats. Indeed, given the pressures for ever larger government, many reformers feel they will have to work hard just to keep it at its present size.

It can't go on 1

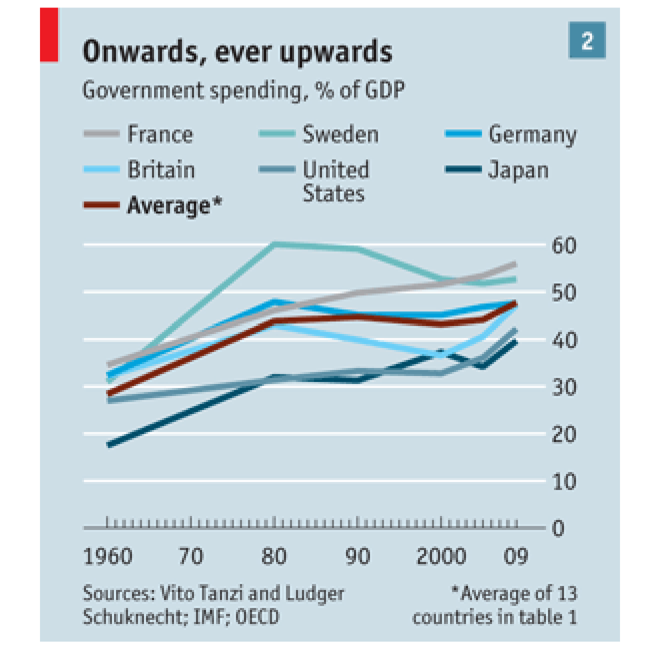
Government* spending, % of GDP

	1870	1913	1920	1937	1960	1980	1990	2000	2005	2009
Austria	10.5	17.0	14.7	20.6	35.7	48.1	38.6	52.1	50.2	52.3
Belgium	*na*	13.8	22.1	21.8	30.3	58.6	54.8	49.1	52.0	54.0
Britain	9.4	12.7	26.2	30.0	32.2	43.0	39.9	36.6	40.6	47.2
Canada	*na*	*na*	16.7	25.0	28.6	38.8	46.0	40.6	39.2	43.8
France	12.6	17.0	27.6	29.0	34.6	46.1	49.8	51.6	53.4	56.0
Germany	10.0	14.8	25.0	34.1	32.4	47.9	45.1	45.1	46.8	47.6
Italy	13.7	17.1	30.1	31.1	30.1	42.1	53.4	46.2	48.2	51.9
Japan	8.8	8.3	14.8	25.4	17.5	32.0	31.3	37.3	34.2	39.7
Netherlands	9.1	9.0	13.5	19.0	33.7	55.8	54.1	44.2	44.8	50.0
Spain	*na*	11.0	8.3	13.2	18.8	32.2	42.0	39.1	38.4	45.8
Sweden	5.7	10.4	10.9	16.5	31.0	60.1	59.1	52.7	51.8	52.7
Switzerland	16.5	14.0	17.0	24.1	17.2	32.8	33.5	33.7	37.3	36.7
United States	7.3	7.5	12.1	19.7	27.0	31.4	33.3	32.8	36.1	42.2
Average	**10.4**	**12.7**	**18.4**	**23.8**	**28.4**	**43.8**	**44.7**	**43.2**	**44.1**	**47.7**

Sources: Vito Tanzi and Ludger Schuknecht; IMF; OECD

*1870-1937 central government, 1960-2009 general government

Government has always tended to expand (see table 1), and people have always fretted about it. In 1888 a French economist, Pierre Paul Leroy-Beaulieu, calculated that a share of 12-13% of GDP (just above the Western average then) was the sustainable limit for a modern state. By 1960 sprawling welfare states had pushed the average in the rich world to 28% (see chart 2), enough to convince Friedrich Hayek that "the deliberately organised forces of society [ie, government regulation]" might "destroy those spontaneous forces which have made advance possible." Yet the next quarter-century saw another surge, pushed mainly by transfer payments and subsidies ostensibly aimed at the poor but often of most benefit to the middle classes.



This sparked a counterblast to halt Leviathan, led by Ronald Reagan and Margaret Thatcher. By the 1990s many people thought that global capitalism would stop the state's advance. This was the decade, after all, when Bill Clinton and other leaders declared the end of big government; when left-wingers claimed (inaccurately) that half the world's biggest economies were multinational firms; when the emerging world was embracing the Washington consensus of deregulation: and when industrial policy mainly meant hanging on to golden shares in privatised companies. A special report in this newspaper, published in 1997, examined the then fashionable idea that the state was withering away. Its author, Clive Crook, now at the *Financial Times*, argued that it was not.

He has been proved right several times over. In continental Europe, where the state's share of the economy was already pretty big, it has not risen that much. However, in America a Republican, George Bush, pushed up spending more than any president since Lyndon Johnson. In Britain New Labour became even less parsimonious: the state's share of GDP rose from under 37% in 2000 to 44% in 2007; with the British economy struggling, it then jumped to 51% in 2010.

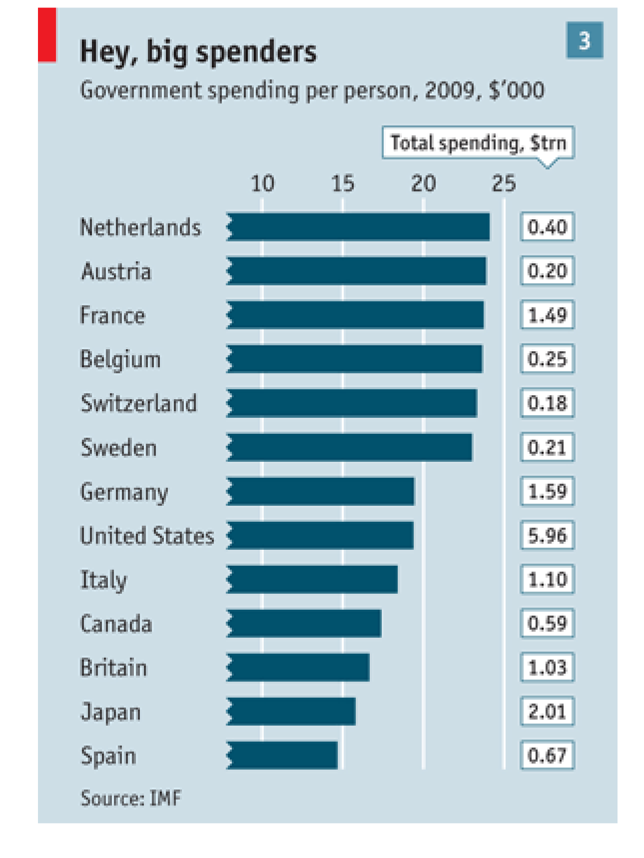
Share of GDP is not the only way to measure state power. "Big governance" can be just as costly to an economy as big government. Some 1,000 pages of federal regulations were added each year Mr Bush was in office. A quarter of a million Americans have jobs devising and implementing federal rules. The European Union has also produced a thicket of red tape. Some are prompted by the left (diversity, health and safety), others by the right (closed-circuit cameras, the war on drugs).

Or look at the state's role in business. In the 1990s privatisation seemed to have settled that argument. Now state capitalism has returned, sometimes accidentally (several banks have become government-controlled) but often intentionally. Many of the new industrial champions of the emerging world are state-owned, and industrial policy is no longer a rude expression even in Anglo-Saxon countries.

There is a belief in boardrooms and among America's tax-cutting right that a monstrous, ever-growing state is the creature of make-work bureaucrats and leftist politicians, and sometimes that is true. But often the beast is responding to popular demand. Globalisation, for instance, has increased many people's reliance on the state: greater job insecurity among the middle classes has increased the calls for bigger safety nets, and the greater inequality that comes with bigger markets has made voters keener on redistribution. Or look at the threat of terrorism, to which the knee-jerk response on America's right was to build up the government in Washington. As Stephen Walt, a professor at Harvard, puts it, "when September 11th happened, nobody rang Bill Gates or the Open Society Institute."

The next battle

The recent advance of government is once again prompting a fightback. The Republicans' victory in the 2010 mid-term elections was hailed as a return to small-government conservatism. Bruised rather than reinforced by his huge health-care reform, Mr Obama is limping back to the centre, suddenly promising businesspeople that he will rein in regulation. In Britain Mr Cameron's government is pushing ahead with reforms that will slim some departments by a fifth. And even in big government's continental European core, private-sector workers are reacting with fury to the perks their public-sector cousins enjoy at their expense. The German Language Society's word of the year for 2010 was *Wutburger* (irate citizen).



But will this fury stop Leviathan's advance? Some scepticism is in order. None of the continental European government-slashers is really trying to change the structure of the state. Mr Cameron's attempt offers a better chance of genuine radicalism, though even his savagery will take back the size of Britain's state only to its level in 2008. The tea-party Republicans seem to be all milk and no caffeine: their first budget proposal did not touch defence or the three great entitlement programmes, Medicare, Medicaid and Social Security. Like the apocryphal sign at a tea-party rally last year, warning government to keep its "hands off my Medicare", they are refusing to confront reality.

Nor is it just spineless politicians who are at fault. A lot of economic theorists have predicted an ever larger state since Adolph Wagner linked its growth to industrialisation in the 19th century. The Baumol cost effect is often cited. In the 1960s William Baumol and William Bowen used the example of classical music to show that some activities are not susceptible to improvements in labour productivity. You still need the same number of musicians to play a Beethoven symphony as you did in the 19th century, even though real wages for musicians have risen since then. Larry Summers, Mr Obama's main economic adviser till the end of 2010, argues that the goods governments buy, especially health care and education, have proved much more resistant to productivity enhancements than the rest of the economy. Since the 1970s real wages in America have risen tenfold if you measure them against the cost of televisions; set against the cost of health care, they have gone down.

Mr Summers expects that trend to continue. An ageing population will need ever more health services provided by the state. Better education means longer school years, smaller classes and more after-school activities, all of which cost more. Greater inequality will mean greater redistribution. In Italy and France cash social transfers alone take up 19% of GDP. The pressure to spend more is continuous, Mr Summers points out, whereas things that reduce the size of government tend to produce one-off savings: the end of the cold war, for instance, took a slice out of defence spending, but that was it.

Mr Summers has a lot of history on his side. This special report takes a more optimistic view. To start with, it is not inevitable that spending will keep on going up. Countries such as Canada and Sweden have reduced public spending when they had to. Moreover, some governments are massively more efficient than others, and there are huge gains to be achieved merely by bad governments copying what good governments do-such as planning ahead, backing winners and rewarding people for doing the right thing. With a smaller central core and much more competition for the provision of services, most governments could do the same for much less.

Most of this special report will focus on that overdue reorganisation. A second set of reforms, for which there is still less political appetite at the moment, would retarget government spending-especially adjusting social transfers (a category that in America's national accounts rose from 8% of GDP in 1970 to 16% in 2009). Benefits that have become middle-class boondoggles should be redirected at the poor.

Not all of history is on the pessimists' side. Fifty years ago companies seemed to be getting bigger and bigger. Business has since changed shape dramatically. The state can catch up by doing many of the same things business did to transform itself, not least bringing in competition and rethinking what it should do itself and what it should contract out to others. And the state, too, has changed shape in the past. In 19th century Britain, for instance, liberal reformers dismantled the patronage state of rotten boroughs and bought offices, building up a professional civil service. Government got leaner and much more efficient. It can surely do so again.

Second, even if Mr Summers is right that the state is unlikely to shrink, there is still a vast amount of work to be done to make it deliver more for the same money and become much more accountable. The ramifications are huge-for people, the economy and society.

Reasons to change

On a personal level, the state matters because it has a big impact on people's lives. As Geoff Mulgan observes in his excellent book on the state, "Good and Bad Power", the quality of the state you live in will do more to determine your well-being than natural resources, culture or religion. In the surveys that measure people's happiness, decent government is as important as education, income and health (all of which are themselves dependent on government).

To business, government can make an enormous difference. Most obviously, if the state accounts for half the economy then improving any part of that will create better conditions for growth. Even if government were to cost the same but produce more (better-educated workers, decent health care, roads without holes, simpler regulation), the effect on private-sector productivity would be electric.

For society, the debate about the state matters because liberalism is on trial. "The challenge of Western democracy is always presented as one to do with transparency and accountability," reflects Tony Blair, who served as Britain's prime minister for ten years. "In fact it is really a challenge of efficacy. Our politicians on the whole are not corrupt. But they are not delivering the services people want. The emerging world is deciding what sort of government it wants. It looks at us and sees a system that costs a lot and does not deliver enough." Another prominent Western politician goes further, seeing government as an increasing problem for the West too. "If it carries on as it is, eventually our own voters may also be more tempted by 'something that makes the trains run on time'."

A host of books have recently been singing the praises of China's authoritarian approach. This special report will look at that model, but it will focus on the rich world, where most of the problems and solutions are to be found. No place better illustrates the troubles of the public sector than California, the American state that has become synonymous with private-sector ingenuity.

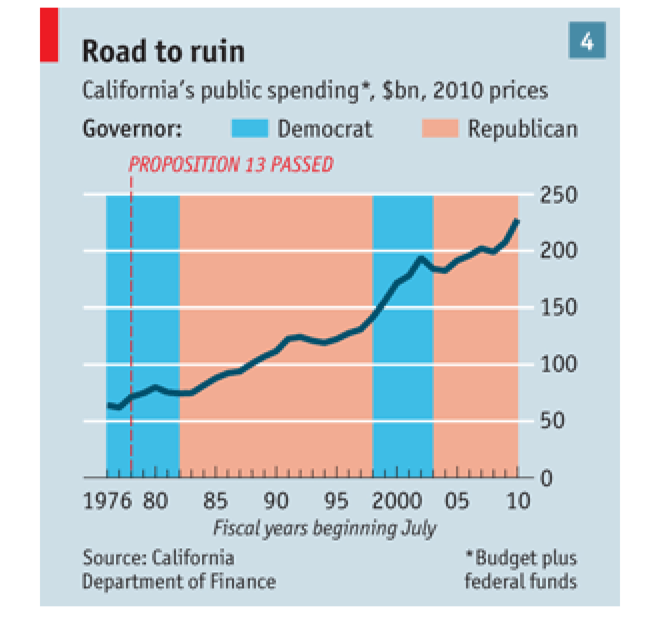
Listen to an interview with the author of this special report

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A special report on the future of the state

California reelin'

Lessons from a place that combines most of the shortcomings of the modern Western state



DON NOVEY does not look like a typical Californian entrepreneur. The grandfatherly, fedora-wearing conservative began his career as a correctional officer at Folsom State prison in the 1970s. But he helped build one of the Golden State's largest industries.

Thirty years ago, when Mr Novey became president of the California Correctional Peace Officers Association (CCPOA), only 2,600 members walked what he calls "the toughest beat in the state", and there were only 36,000 inmates in California's prisons. Now, as Barry Krisberg of Berkeley Law School points out, some 170,000 people are locked up there, and CCPOA has 31,000 members. From the air California can look like an archipelago of prisons.

Mr Novey made CCPOA a dominant force in state politics, and not just by dishing out political contributions in Sacramento, the state capital. He shrewdly formed an "iron triangle" with Republican lawmakers and prison-builders. And he gave it a cause: tougher sentencing for criminals. CCPOA sponsored the "three strikes" law, mandating life imprisonment for three serious felonies, and helped set up victims' rights groups.

By the time Mr Novey gave up the CCPOA's presidency in 2002, the state had built 21 new prisons. Some guards now earn more than $100,000 a year (with overtime). Mr Novey negotiated pensions of up to 90% of salary, with retirement starting as early as 50. To many of his members Mr Novey remains a hero-a man who provided good jobs and made them safer. And the taxpayer footed the bill.

Jerry Brown, the Democrat who was recently elected governor, faces a deficit of around $25 billion this year-bigger than the total budget in 1975. That was the year when Mr Brown in his younger "Governor Moonbeam" phase first ran the state. Back then California's government was widely admired for its highways and its universities, and also as a font of political ideas both on the right (Reaganism) and the left (environmentalism). Now the roads and colleges are crumbling, even though total government spending in the state will reach $230 billion this year (see chart 4). Californian politicians get some of the lowest ratings in the country. Like a paranoid movie star, the state has kept on grasping at miracle cures-from Proposition 13, the tax-cutting ballot initiative, in 1978 to the election of Arnold Schwarzenegger, the cyborg-ex-machina, in 2003.

California is now widely studied as an example of what to avoid. Why is the home of Apple and Google so useless when it comes to running school districts or budgeting, and why have so many clever people settled for such a bad deal? Such questions are worth asking because what happens in California, which is famously like America, only more so, tends to happen elsewhere. And indeed a list of its ailments applies to a greater or lesser extent throughout the Western world.

â€¢ **A messy structure of government.** Look at an administrative map of California and you might assume that a child had scrawled over the design. It is a muddle of thousands of overlapping counties, cities and districts. Beverly Hills and West Hollywood sit in the middle of Los Angeles but are separate cities. The LA school district has 687,000 pupils, but there are 23 others with 20 pupils or fewer. Often voters have little idea what their officials do for their money. Last year the residents of Bell, a poor Latino city of 38,000 people, found their city manager was paid $788,000 and their police chief $457,000 a year.

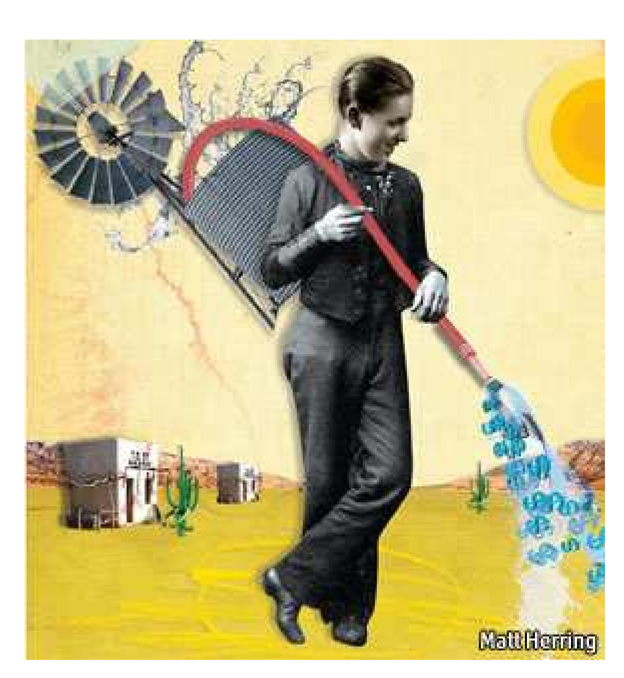
In Sacramento things are no clearer. Thanks to various voters' initiatives, as much as 75% of the budget is outside Mr Brown's control. Proposition 13, which halved and capped property taxes, forced the state to bail out local government. A chunk of the state's own money comes from the federal government. So cash for health, schools, welfare and much else sloshes backwards and forwards between Sacramento, Washington and various Californian cities. That makes it impossible to hold any Californian politician fully accountable for any part of government.

Some of this stems from specifically Californian afflictions, especially the ballot initiatives. But overlapping areas of responsibility are common throughout the West. In Australia, for instance, the federal government runs primary health care but the states run hospitals. In most European countries taxes are raised centrally but tend to be spent by local or regional government. The European Union increasingly plays the same role that Washington does in America, adding another layer of rules and mandates.

â€¢ **Out of date.** The most recent full redesign of California's government was in 1879, when the state had only 865,000 people; now it has 37m, and a single state Senate seat represents more people than the whole Senate did then. As California's pre-eminent historian, Kevin Starr, observes, "it is not surprising that an organisation set up to look after fewer than a million people should have a collective political nervous breakdown when it governs something almost 40 times that size."

The same argument could be applied to the United States as a whole. Its constitution was designed for a country of 13 states and 4m people, when things like religious tolerance, the right to form militias and preventing people trying to become king mattered a lot. The Founding Fathers had no plans to bring either North Dakota or California into their union, nor could they imagine the ramifications of those two states both having the same voting weight in the Senate even though California's population is 57 times bigger.

In Europe, thanks in part to two world wars, the state has been redesigned more recently, though many antiquated structures-such as Britain's House of Lords-have survived. Many of these oddities work well in practice, and Americans revere their constitution. But structure matters. It is hard to think of any successful commercial outfit that has stuck to the same organisational design for 23 years, let alone 230.



â€¢ Too much power for vested interests. In "The Logic of Collective Action" (1965), Mancur Olson argued that rational individuals will work hard in a group with a selective aim reserved for its members (prison guards banding together to press for higher wages, for instance); they will expend less energy to push for public goods whose benefits are widely shared. Once entrenched, an interest group is extremely hard to shift. Its members have much to gain by fighting to retain their particular privileges, and would-be reformers have to take on disproportionately large costs to push for a vaguer public good. Californians have moaned about their prison guards' perks for a while, yet have only recently plucked up the political will to do anything about them.

In rich countries no group has illustrated Olson's work more clearly than farmers. In California's Central Valley you can watch Californian tax dollars evaporating before your eyes as farmers guzzle most of the state's precious water to cultivate crops that were never meant to grow in a desert. In the European Union two-fifths of the budget still goes to agriculture. In Poland farmers are exempt from income tax. Just as with the prison guards, the subsidies keep flowing to farmers largely

because of conservative politicians. Although the greediest public-sector unions are firmly allied with the left (see article), the supposedly low-tax right also lavishes money on its own priorities. The new Republican leadership in Washington started its search for waste in the foreign-aid budget by trying to get the biggest recipient of American largesse, Israel, moved to the Pentagon's budget.

Interest groups work especially well in systems like America's where money needs to be raised and where party primaries matter. A Republican politician describes how the gun lobby works. If a Republican congressman signs up to the National Rifle Association's agenda, he gets a little money and some organisational help from vocal supporters. If he does not, the NRA will put a lot of resources behind his opponent in the primary. Going with the NRA is thus a lot easier. Many Democrats would say exactly the same about the teachers' unions and education reform. Opposing them is not worth the hassle.

Olson's theory also helps explain why broad-based lobbying by big business has given way to narrower special interests. Fifty years ago California was run by a business elite, keen to keep taxes down and infrastructure spending up but with a broad interest in the well-being of the state. Since then Californian businesspeople have discovered that targeted lobbying can do a lot for their specific business. That has made it harder to get commercial interests to support projects of general benefit such as transport in the Bay area. It has also brought about an increase in regulation as individual businesses have lobbied for rule changes that create barriers to entry for other firms.

â€¢ Ever more rules and taxes. A study last year by the Pacific Research Institute said California had the fourth-largest government of all American states, with state and local spending equal to 18.3% of its gross state product. Texas, a state with which California is often compared, chewed up just 12.1% of GSP. It also looked at tax structures, and on that count California came 45th out of 50 states, with its steep income tax being especially damaging. Its tax system has been a mess ever since the dotcom boom when it relied too heavily on capital-gains taxes. As taxpayers have got crosser, the state has tried to tax them as sneakily as possible while adding tax breaks for favoured lobbies.

This points to two endemic problems with government throughout the West. The narrow one is that tax systems are in need of reform. America's tax code has grown from 1.4m words in 2001 to 3.8m in 2010. Members of the European Union, too, have made their tax systems increasingly complicated-with the heroic exception of flat-tax Estonia. Most economists think taxes should be shifted towards consumption and away from income and investment. But whatever the system, it should be easy to understand.

The broader problem is the growing thicket of regulation-of which taxes are merely the most onerous part. Many of the new laws that have been passed in both Europe and America have admirable aims: better health care, cleaner air, less discrimination against minorities. But as Philip Howard of Common Good points out, they are amazingly cumbersome-Mr Obama's health bill was over 2,000 pages long-and once on the statute book, they seldom come off again. One solution is to follow Texas's example and let legislatures meet only occasionally. Another would be to introduce sunset clauses so that all regulations automatically expire after a while.

â€¢ The politics of gridlock. Sixty years ago California's politics were rather cosy. In the early 1950s Pat Brown, Jerry's father, who was then the Democratic attorney-general, used to share a car from Sacramento to San Francisco on Fridays with Earl Warren, the Republican governor. This year Jerry Brown in his inauguration speech described politics as a primordial battle between "Modocians" and "Alamedans" (Modoc being a rural, conservative Republican county and Alameda a liberal enclave east of San Francisco).

It is fashionable to blame this animosity on the internet and on partisan media channels such as Fox News. But it often has structural causes, such as gerrymandering. California has tended to choose centrists-liberal Republicans or conservative Democrats-in statewide elections, but the legislature's electoral boundaries have been drawn to produce the biggest number of safe seats. That means primaries are the only real test for most politicians. Here reform may at last be on the way: Mr Schwarzenegger managed to force through an initiative that handed over redistricting to an independent commission.

But at a national level it will be a long time before America has a sensible debate about its budget deficit. George Lodge, a Harvard Business School professor who ran as a Republican against Ted Kennedy in Massachusetts in 1962, argues that many Western countries are now conducting a dialogue of the deaf. Conservatives want to talk about the "macro" vision (a smaller state) but not the "micro" specifics (the unpopular cuts to achieve that). Leftists want to talk about specific micro programmes they want to build up without ever discussing the macro bill for all of them.

â€¢ **Towards the older middle.** Given the fury from the left about bankers and from the right about welfare spongers, you would expect all that extra government spending to have been swallowed by either end of the income spectrum. In fact in California, as in most of the West, the cash has flowed mostly towards those with middle incomes and the old.

Both the rich and the poor do relatively badly out of government. The rich pay for most of it. In California the top 1% by income accounted for 43% of income-tax revenues in 2008 and the top 5% paid 64%. In America as a whole the top 1% paid 38% of federal income taxes and the top 5% paid 58%; their respective shares of national income were 20% and 38%. The wealthy pay the lion's share in most European countries too. Getting the rich to cough up so much might be a desirable social goal in a time of great inequality, but it is hard to claim that they are not paying their share.

The poor pay virtually no income taxes, and many countries, especially in Europe, have a problem with entrenched welfare dependency. Britain, for instance, has a quarter of a million households in which no one has ever held a formal job. But overall it is not clear that the poor benefit from government transfers and benefits as much as you might expect. In America two-fifths of all "social payments" are made by the private sector through employers' pension contributions and health plans-both spurred on by tax breaks that go mainly to middle-income Americans.



When you look at overall public spending, the gap widens. Middle-income Californians go to better schools than poor ones do. Their streets often have more policing. They are far more likely to go to a publicly financed university, to claim mortgage relief on their home, to own a farm that collects subsidies or to attend a ballet supported by public funds. Europe is different only in that it subsidises the middle classes less through tax breaks and more through "universal" benefits-things like free bus passes for the old-which often started out being targeted at the poorest but are now given out to all.

That points to another distortion, which is generational. A large number of welfare payments and social transfers are now aimed at the elderly. The huge baby-boom generation that is just about to retire will make these even more expensive. In Christopher Buckley's political satire, "Boomsday", America's young eventually start bribing their self-indulgent parents to end their lives early. In his interesting book "The Pinch", David Willetts eschews that solution for Britain's baby-boom generation, but calculates that it will take out nearly 20% more from the system than it has put in. The first budget of the new Tory government, in which Mr Willetts is a minister, still directed money disproportionately towards the old.

Across the rich world, politicians keep on pushing money towards the middle class and the old because that is where elections are decided. People aged 65 and older still account for only 13% of America's population, but they made up over a fifth of its electorate in 2010. No group is better organised: the AARP (formerly the American Association of Retired Persons) has 40m members.

â€¢ **The secession of the successful.** Hollywood, Silicon Valley or any of the other places where successful Californians gather show a profound contempt for their government. At the most extreme, such people have walled themselves off in gated communities, with their own security, health services and even schools. Their main relationship with the state, at least as they see it, is to write a cheque for their taxes-and their only interest in it is that the cheque be as small as possible. Philanthropy continues, but remarkably little goes into beautifying their environment (Silicon Valley is the ugliest industrial cluster imaginable).

Similar complaints can be heard in other centres of elitism: Wall Street does not do much about the Bronx, and the City of London usually ignores the East End. Both globalisation and the internet have increased this sense of separation. Companies with strong local links have been swallowed up by larger groups. Wells Fargo used to be a powerful force in San Francisco and Security Pacific in Los Angeles; both are now part of bigger empires. The Indian tycoons in Palo Alto feel closer to Bangalore than they do to Bakersfield (and so do many of their American colleagues).

This secession has an effect on government. It makes capital, as well as businesses and talented people, more footloose, so it becomes harder to raise taxes overtly. Worst of all, the secession of the successful means that the most talented brains are largely left out of the mix. One leading California Democrat describes the list of businesspeople prepared to run a public commission as "painfully short".

â€¢ **You, yes you, are to blame**. California is interesting for one final reason. Throughout most of the West, people are in denial about the consequences of wanting both more government and lower taxes. In California ballot initiatives have actually given voters a direct say. Generally they have made government worse, protecting bits of spending yet refusing to pay for it. Having voted for Mr Schwarzenegger in 2003, they deserted him the moment he tried to introduce structural reforms in 2005.

Interviewed shortly before his exit at the start of this year, the gubernator had two thoughts. One was that his successor would find reform easier because the system is more manifestly bust now than it was in 2003 (and Mr Brown is certainly having a go). The other is that Californians are still determined to get something for nothing. "People here are addicted to improving their lifestyle. They want more and more from their government."

Is there a better way? Many of those who used to see the future in the Golden State now prefer to look across the Pacific-towards emerging Asia.

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A special report on the future of the state

Enemies of progress

The biggest barrier to public- sector reform are the unions

IF JIMMY HOFFA were reincarnated as a modern trade unionist, he would probably represent civil servants. When Hoffa's Teamsters were in their prime in 1960, only one in ten American government workers belonged to a union; now 36% do. In 2009 the number of unionists in America's public sector passed that of their brethren in the private sector. In continental Europe most civil servants belong to unions, though these generally straddle the private sector as well. In Britain more than half of public-sector workers but only about 15% of private-sector ones are unionised.

There are three reasons for the public-sector unions' clout. First, they can shut things down without suffering much in the way of consequences. Second, they are mostly bright and well-educated. There are some Luddites left, such as Bob Crow of London's perennially striking Tube drivers. But it is much harder to argue with Randi Weingarten, the articulate head of the American Federation of Teachers. Most workers in the public sector are women, and many of them are professional types. A quarter of America's public-sector workers have a university degree. Officers of the British Medical Association (which represents doctors) and America's National Education Association (the biggest teachers' union) often appear on the news as experts on health and education rather than as representatives of interest groups.

Third, they now dominate left-of-centre politics. Some of their ties go back a long way. Britain's Labour Party, as its name implies, has long been associated with trade unionism. Its current leader, Ed Miliband, owes his position to votes from public-sector unions. Spain's prime minister still likes to brandish his union card. In America the links have become more explicit. Between 1989 and 2004 the biggest spender in federal elections was the American Federation of State, County and Municipal Employees, and $39.4m of the $40m it shelled out over that period went to Democrats. One in ten of the delegates at the 2008 Democratic National Convention in Denver was a teacher.

At the state level their influence can be even more fearsome. Mark Baldassare of the Public Policy Institute of California points out that much of the state's budget is patrolled by unions. The teachers' unions keep an eye on schools, the CCPOA on prisons and a variety of labour groups on health care. It was the big public-sector unions which squashed the 2005 reforms proposed by Arnold Schwarzenegger, then California's governor.

In many rich countries average wages in the state sector are higher than in the private one. But the real gains come in benefits and work practices. Politicians have repeatedly "backloaded" public-sector pay deals, keeping the pay increases modest but adding to holidays and especially pensions that are already generous.

Many Germans were horrified to discover that the EU rescue package for Greece last year helped to bail out public-sector workers who could retire in their mid-50s on almost full pay. One scam in American cities has been to link pensions to employees' earnings in their final year, rather than average earnings over a longer period. Naturally the subway drivers or policemen concerned put in heroic overtime in that final year.

Reform has been vigorously opposed, perhaps most egregiously in education, where charter schools, vouchers, academies and merit pay all faced drawn-out battles. Even though there is plenty of evidence that the quality of the teachers is the most important variable, teachers' unions have fought against getting rid of bad ones and promoting good ones.

As the cost to everyone else (in terms of higher taxes and sloppier services) has become clearer, politicians have begun to clamp down. In Wisconsin the unions have rallied thousands of supporters against Scott Walker, the hardline Republican governor. But many within the public sector suffer under the current system too.

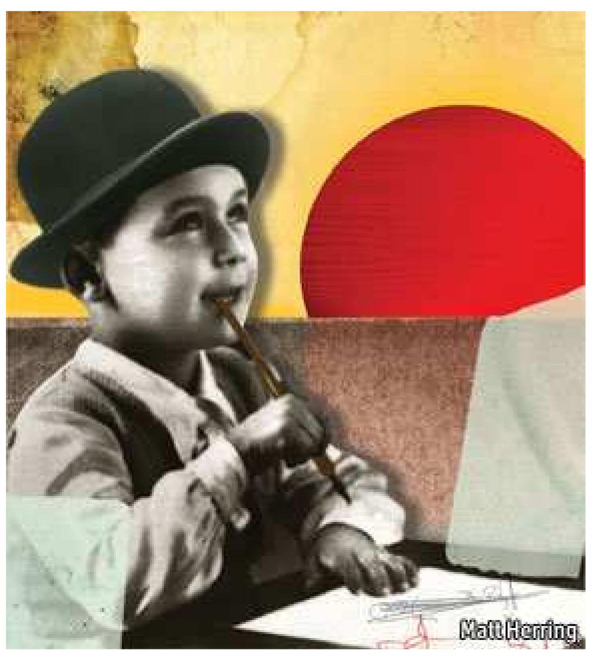
John Donahue at Harvard's Kennedy School points out that the egalitarian culture in Western civil services suits those who want to stay put but is bad for high achievers. Heads of departments often get only two or three times the average pay. As Mr Donahue observes, the only American public-sector workers who earn well above $250,000 a year are university sports coaches and the president of the United States. Hank Paulson took a 99.5% pay cut when he left Goldman Sachs to become America's treasury secretary. Bankers' fat pay packets have attracted much criticism, but a public-sector system that does not reward high achievers may be a much bigger problem for America.

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A special report on the future of the state

Go East, young bureaucrat

Emerging Asia can teach the West a lot about government



WHEN people talk about Singapore's education miracle, they normally think of rows of clever young mathematicians. The hair-design and beauty-therapy training centres at the Institute of Technical Education (ITE) are rather different. The walls are covered with pouting models, L'Oreal adverts and television screens. There is a fully fitted-out spa and a hairdressing salon. It all seems rather more "Sex and the City" than Asian values, though the manicurists, pedicurists, cosmetologists and hairdressers toil diligently.

Asked whether he wants to go to university, the holy grail of most Asian families, a young barber called Noel replies that he would rather open a hairdressing salon. Mei Lien wants to set up her own beauty salon; Shuner would like to work in hotels abroad.

Until recently ITE-dubbed "It's The End" by ambitious middle-class parents-was the dark side of Singaporean education. The city state streams pupils rigorously and is unashamedly elitist: one school claims to send more students to Ivy League universities than any other secondary school in the world. But such a system also produces losers-and many of the bottom third who do not make it to university come to ITE.

Since the 1990s the government has worked hard to change ITE's image. It has not only spent a lot of money on new facilities and better teachers but also put a great deal of thought into it, scouring the West for best practice in vocational training. And it has encouraged students who are used to failure to take pride in their work. That has involved discipline (a list displays the names of class-shirkers) but also fun outside the classroom: ITE has sports teams and concerts just like any university.

This attention to detail has paid off. Many of the graduates have to compete with cheap migrant workers, especially in service jobs, but most of them are snapped up quickly. The hairdressers and beauty therapists are off to the new casinos, or "integrated resorts", as they are prudishly known. Singapore, already near the top of most educational league tables, has created yet another centre of excellence that is beginning to attract foreign visitors.

Singapore is important to any study of government just now, both in the West and in Asia. That is partly because it does some things very well, in much the same way that some Scandinavian countries excel in certain fields. But it is also because there is an emerging theory about a superior Asian model of government, put forward by both despairing Western businesspeople and hubristic Asian chroniclers. Simplified somewhat, it comes in four parts.

First, Singapore is good at government (which is largely true). Second, the secret of its success lies in an Asian mixture of authoritarian values and state-directed capitalism (largely myth). Third, China is trying to copy Singapore (certainly true). Last, China's government is already more efficient than the decadent West (mostly rubbish, see next section).

Fact or fiction?

For all the insults hurled at "Disneyland with the death penalty" (to use William Gibson's gibe), Singapore provides better schools and hospitals and safer streets than most Western countries-and all with a state that consumes only 19% of GDP. Yes, that proportion is understated because it does not include the other fingers the government has in the economic pie, such as its huge landholdings, the Central Provident Fund (a mandatory savings scheme) and Temasek (a government-linked investment company). Yes, it is easier to serve 5m people on a tiny island than 309m Americans on a vast landmass. Yes, it has relied on immigration, which is now creating strains (and will be the main topic in the next election). And yes, Singapore's bureaucrats can make mistakes, such as letting an Islamic terrorist escape in 2008. But its government does pretty well.

The Chinese are fascinated by it. "There is good social order in Singapore," Deng Xiaoping observed in 1992. "We should draw from their experience, and do even better than them." It sends streams of bureaucrats to visit Singapore. One of the first things that Xi Jinping did after being anointed in 2010 as China's next leader was to drop in (again) on Lee Kuan Yew, Singapore's minister-mentor, who ran the island from 1959 to 1990, and his son, Lee Hsien Loong, who has been prime minister since 2004. The Chinese are looking at other places, too-most obviously Hong Kong, another small-government haven. But it is hard to think of any rich-country leader whom China treats with as much respect as the older Mr Lee.

So what lessons are the Chinese learning? There is an odd imbalance between the things that Singapore and others make so much noise about and the reasons why the place works. In particular, the "Asian values" bits of Singapore-its authoritarianism and its industrial policy-that the Chinese seem to find especially congenial are less vital to its success than two more humdrum virtues: a good civil service and a competitively small state.

The island that Lee built

Singapore is certainly a fairly stern place. It has been run by the People's Action Party for half a century. The older Mr Lee, a Cambridge-educated lawyer who was originally seen as a bit of a left-winger, set up a parliamentary system in which it has proved curiously difficult for the opposition to do well. From 1966 to 1981 Mr Lee's PAP won all the seats. It has opened up a bit, and in the most recent election in 2006 it won only 66% of the votes and 82 of the 84 seats. The media, and particularly the internet, have also got a little freer.

The Singaporeans argue that they have the perfect compromise between accountability and efficiency. Their politicians are regularly tested in elections and have to make themselves available to their constituents; but since the government knows it is likely to win, it can take a long view. Fixing things like ITE takes time. "Our strength is that we are able to think strategically and look ahead," says the prime minister. "If the government changed every five years it would be harder."

There is more truth in this than Western liberals would like to admit. Not many people in Washington are thinking beyond the 2012 presidential election. It is sometimes argued that an American administration operates strategically for only around six months, at the beginning of its second year-after it has got its staff confirmed by the Senate and before the mid-terms campaign begins.

Yet even assuming that voters are happy to swap a little more efficiency for less democracy, Singapore still seems a difficult model to follow. Not only is it manageably small, but balancing authoritarianism and accountability comes down largely to personal skills (and even the opposition admits that the two Lees have been extremely good at it). More generally, Singapore's success as a planning state has a lot to do with the sort of people who run it.

One thing that stands out in Singapore is the quality of its civil service. Unlike the egalitarian Western public sector, Singapore follows an elitist model, paying those at the top $2m a year or more. It spots talented youngsters early, lures them with scholarships and keeps investing in them. People who don't make the grade are pushed out quickly.

Sitting around a table with its 30-something mandarins is more like meeting junior partners at Goldman Sachs or McKinsey than the cast of "Yes, Minister". The person on your left is on secondment at a big oil company; on your right sits a woman who between spells at the finance and defence ministries has picked up degrees from the London School of Economics, Cambridge and Stanford. High-fliers pop in and out of the Civil Service College for more training; the prime minister has written case studies for them. But it is not a closed shop. Talent from the private sector is recruited into both the civil service and politics. The current education minister used to be a surgeon.

Western civil services often have pretty good people at the top, but in Singapore meritocracy reigns all the way down the system. Teachers, for instance, need to have finished in the top third of their class (as they do in Finland and South Korea, which also shine in the education rankings). Headmasters are often appointed in their 30s and rewarded with merit pay if they do well but moved on quickly if their schools underperform. Tests are endemic.

How much strategic intervention takes place in the economy? The Lees have dabbled in industrial policy, betting first on manufacturing and then on services. Temasek manages a portfolio of S$190 billion ($150 billion). The country is now trying to push into creative industries, with limited success thus far, as ministers admit.

These attempts at *dirigisme* have made Singapore a more reserved, less entrepreneurial place than Hong Kong with its feverish laissez-faire. It certainly has far fewer larger-than-life billionaires. But it is hard to hail Singapore as a success of top-down economic management in the way some Chinese seem to think. Indeed, the core of Singapore's success-its ability to attract foreign multinationals-owes far more to laissez-faire than to industrial policy.

Come in, the water's lovely

Rather than seeing foreign investment as a way to steal technology or to build up strategic industries, as China often does, Singapore has followed an open-door policy, building an environment where businesses want to be. The central message has remained much the same for decades: come to us and you will get excellent infrastructure, a well-educated workforce, open trade routes, the rule of law and low taxes.

In other words, Singapore's competitive advantage has been good, cheap government. It has worked hard to keep its state small; even education consumes only 3.3% of GDP. But the real savings come from keeping down social transfers and especially from not indulging the middle class. The older Mr Lee thinks the West's mistake has been to set up "all you can eat" welfare states: because everything at the buffet is free, it is consumed voraciously.

Singapore's approach, by contrast, is for the government to provide people with assets that allow them to look after themselves. Good education for all is one big part of it. The other mainstay is the Central Provident Fund. A fifth of everybody's salary goes into their account at the CPF, with the employer contributing another 15.5%. That provides Singaporeans with the capital to pay for their own housing, pensions and health care and their children's tertiary education.



There is a small safety net to cover the very poor and the very sick. But people are expected to look after their parents and pay for government services, making co-payments for health care. The older Mr Lee especially dislikes free universal benefits. Once you have given a subsidy, he says, it is always hard to withdraw it. He is convinced that if you want to help people, it is better to give them cash rather than provide a service, whose value nobody understands. China, he thinks, will eventually follow Singapore's model.

But arguably the place that should be learning most from Singapore is the West. For all the talk about Asian values, Singapore is a pretty Western place. Its model, such as it is, combines elements of Victorian self-reliance and American management theory. The West could take in a lot of both without sacrificing any liberty. Why not sack poor teachers or pay good civil servants more? And do Western welfare states have to be quite so buffet-like?

By the same token, Singapore's government could surely relax its grip somewhat without sacrificing efficiency. That might help it find a little more of the entrepreneurial vim it craves.

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Favelous

Sometimes the best ideas for government are the simplest

HELIÃ“POLIS sounds a rather futuristic place. In fact Sao Paulo's biggest *favela* (slum) crams some 200,000 people into a small area just below a road called the Street of Tears. Despite its obvious poverty, it seems fairly law-abiding. Even though they don't pay taxes, the cafes enforce a 2009 smoking ban. A gym full of predictably skilful football players has plaques celebrating its two most famous visitors: Zinedine Zidane, of Real Madrid fame, and Luiz Inacio Lula da Silva, Brazil's president from 2002 to 2010.

Lula remains a folk hero. Posters from the election last year show him endorsing his less charismatic successor, Dilma Rousseff. The other thing that rallied Heliopolis to Ms Rousseff's cause was the (unfounded) rumour that her opponent

was going to scrap Bolsa Familia, Brazil's conditional cash-transfer programme. It works because it is simple: poor families get cash if they send their children to school and take them for health checks.

Outside a creche stand three claimants, all migrants from the north-east. Maria Lucineide has three children, Marcia four and Maria Lucia five, entitling them to 66-112 reais ($40-68) a month, but Maria Lucia's children skipped school and now she gets nothing.

A nudge in the right direction

The money from Bolsa Familia goes on small luxuries-sweets or snazzier sneakers. But it is enough to make a difference. "If you don't go to school, you are going to be a nobody," Maria Lucineide lectures her children. "And it will also mean that we can't buy the things that you like." Asked for their views on the state, the three mothers, who missed out on education themselves, give an answer you would rarely hear in the rich world: "Government is wonderful."

Bolsa Familia goes to 13m families, around one in four. It has had a fairly dramatic effect on poverty and inequality. Marcelo Neri, a Brazilian economist, attributes 17% of the narrowing in inequality since 2001 to the programme: pensions and other welfare payments had a similar effect, but at a massively higher cost. He thinks it should be extended to students to improve their grades as well. It also counts as a form of affirmative action, since a disproportionate amount goes to blacker Brazilians.

It is not universally popular. Snooty Paulistas whinge about the "Bolsa Miseria" going to the undeserving poor. And it may work better in the countryside than the cities. Jonathan Hannay, who has worked with Brazilian street children for 17 years, thinks that Bolsa, which has absorbed other social programmes, has reduced their impact significantly.

Against that, Bolsa Familia is very cheap, costing only about 0.4% of GDP. And it is a paragon of efficiency when set beside the rest of the Brazilian state, which although of first-world size (eating up 40.9% of GDP in 2008) delivers third-world services, such as a legal system that cannot enforce contracts. Much of this is down to the perks of public-sector unions. Teachers have the right not to turn up to work for a set number of days a year-and enjoy some of the world's cushiest pensions. Ms Rousseff has pledged reform, but half the country's civil servants are members of her party.

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A work in progress

China's government is much less impressive than many Westerners believe

IF THERE was one thing that the world's tycoons agreed on at this year's World Economic Forum in Davos, it was that the Chinese state is a paragon of efficiency-especially compared with the doltish, venal clowns in Washington and Brussels. "Beijing really gets things done," sighed one American chief executive. "Their government people are so much smarter: it's terrifying," enthused one of the world's richest men. The chalets resounded with stories of contracts rapidly signed, roads speedily built and young engineers designing brilliant cars and software programs.

There is indeed much to admire about parts of the Chinese government. Over the past 30 years the regime has overseen perhaps the biggest increase in economic well-being ever, with several hundred million people moving into the middle class (even if the state had previously been the main thing that held them back). China is led by a group of people who take government enormously seriously.

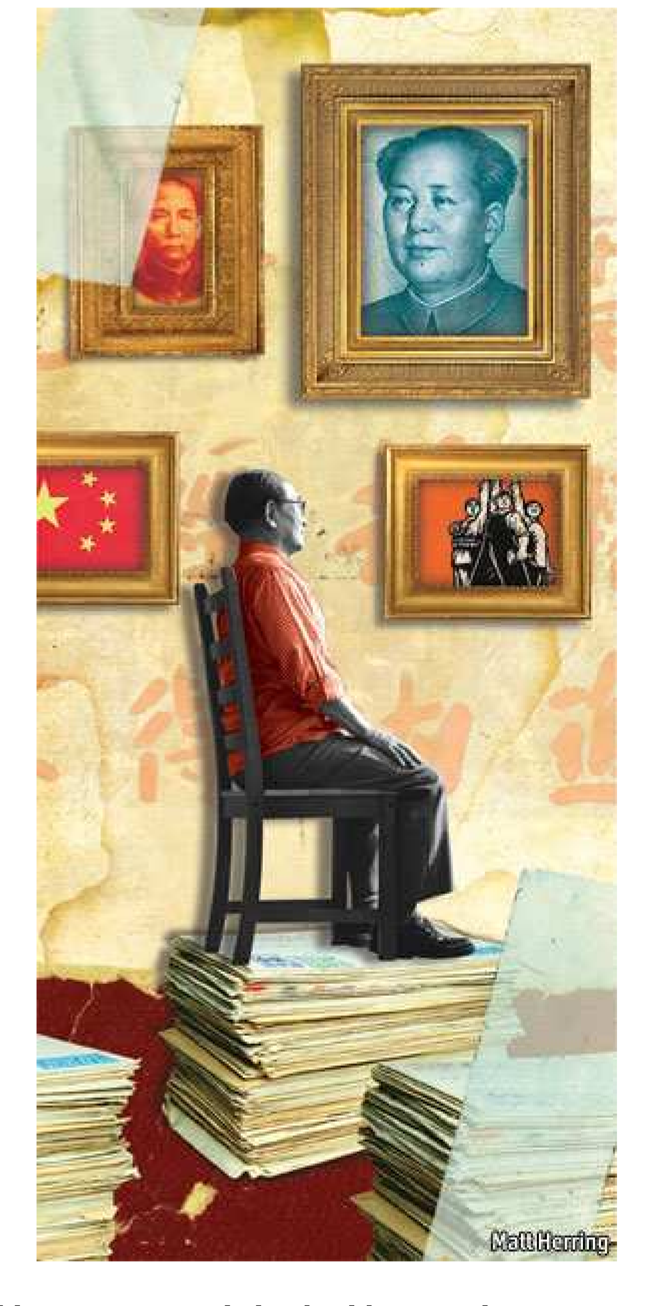
For all this, there is something of a Potemkin village about the Chinese state. It is, after all, not terribly hard for a dictatorship to build roads and railways faster than a democracy can. Multinational companies and the educated middle classes are doing well from the state, but the poorer majority in this ever more unequal country get a raw deal. And even if some of its leaders are trying to move closer to Singapore's model, there are countless stronger forces pushing in the opposite direction.

Begin with the part of the Chinese state that is winning most praise abroad at the moment: education. In the recent rankings of school students by the OECD's Programme for International Student Assessment (PISA), Shanghai hurtled to the top in mathematics, science and reading, ahead of more than 60 other countries. China is also being cited as the coming force in universities. The number of higher-education institutions has more than doubled in the past decade, from 1,022 to 2,263. The number of students enrolled in degree courses has risen from 1m in 1997 to 5m.

Behind this gleaming facade, however, not everything is what it seems. The new universities are real enough, though they remain middle-class bastions: very few of China's poorer citizens get a look-in. But China's schools are not as uniformly good as Shanghai's miraculous PISA performance suggests. Investment remains low, even by developing-country standards. As far back as 1993 the state pledged to spend 4% of GDP on education: in 2006 the figure was still 2%, and the 4% target was put back first to 2010 and now to 2012. *China Youth Daily*, an organ of the Communist Youth League, has observed that China spends five times more on wining and dining local-government officials than it does on educating children up to 16.

The schools in the countryside are particularly bad. The recent abolition of fees has meant that more pupils now attend them, but it has also prompted local governments to cut back on full-time teachers. In the cities more money is spent, though it still usually takes a backhander to get a child into a good school. And many of the poorest children in the cities miss out on public education of any sort.

One example of this is indirectly provided by Shenzhen's new civil society: a school for the children of migrant factory workers set up by the Ciwei Philanthropy Institute. The school buzzes with endeavour. It looks after 132 children who cannot go to the city's schools because their parents, many of whom work for a nearby nuclear plant, are from out of town. That might seem fair enough for the children of temporary workers, but virtually all the pupils at this school were born in Shenzhen and have lived there all their lives. They are part of a permanent majority. Out of Shenzhen's population of more than 14m people, only 2.5m are residents.



These "black" workers and their children are not entitled to health care, education or pensions in the city because their *hukou* (residence registration) is elsewhere. In theory you can transfer your *hukou* from one place to another. With enough documentation, any child under 15 should be able to get free education in Shenzhen. But it is a fiendishly complicated and corrupt business, and many migrants don't have the right papers. Some leave their children behind; others cough up for the 70 or so rudimentary private schools in the city. That saves Shenzhen's mainly middle-class residents and the foreign companies based there a lot of taxes, but it also creates an almost apartheid-like class system.

Much of the rest of Chinese local government is similarly skewed against the agrarian poor. Most of the main Chinese taxes go to Beijing; the central government then sends some money back to the provinces, and from there it trickles down through the prefectures to the lower levels of local government that are responsible for basic services. Chinese cities make ends meet through land-grabs. Property on the edge of town is bought, using compulsory-purchase orders that seldom pay the landowners properly, and then sold to developers, who sell on the houses they build to the richer urban middle classes. *Caixin*, a magazine, reported recently that revenue from land-rights sales made up 46% of all local-government revenue. That hardly seems sustainable.

The perils of making a fuss

Many people are angry about the quality of public services, as Yang Jianchang has found. He is in charge of the Luohu District Office of Market Supervision (Industrial and Commercial Bureau), which deals with counterfeiting; musty signs outline the penalties for producing fake Hermes bags. But Mr Yang, a deputy in Shenzhen's Municipal People's Congress, is best known for being China's most accountable representative.

In 2005 he took the unusual step of opening a separate personal office. People and mail flooded in, mostly complaining about the government. Over the past five years he has taken up 3,000 cases on behalf of some 20,000 people. He has been

threatened and roughed up; his health is poor. Some of the villains and bureaucrats whom he pursued-for instance, for selling unsafe food-have gone to prison. Many more have not (thanks to the intervention of what people in Shenzhen describe as "powerful interests"), but he has usually caused enough fuss for them to stop whatever they were up to.

Mr Yang is a proud party man: his office is adorned with pictures of him in his uniform and with citations from various Communist dignitaries. You might imagine that a regime on an anti-corruption drive might embrace this example of accountable government. But last October the National People's Congress passed a law in effect banning deputies from setting up personal offices. The law applies across the country, and it seems to have been drawn up to stop people like Mr Yang. He has closed his personal office but mail continues to flood in, most of it by recorded delivery, so people know he has got it and will send it on to the right bureaucrat.

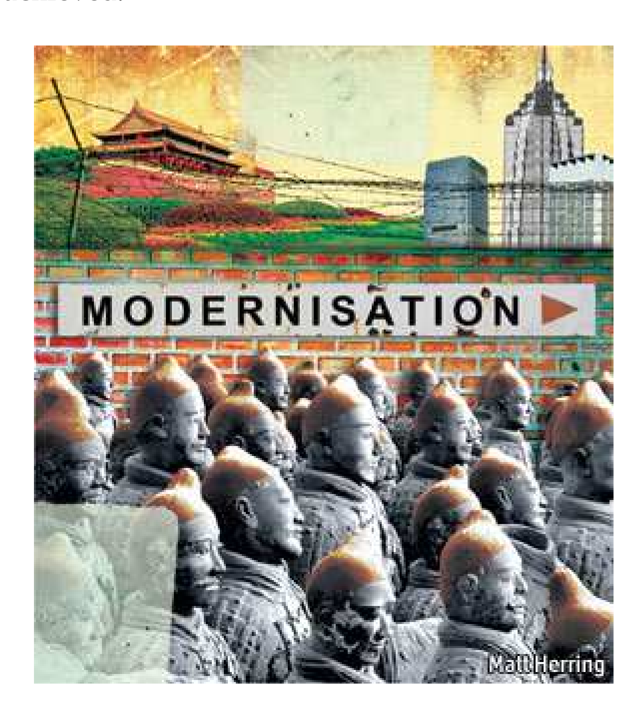
All this points to the sheer unresponsiveness of much of China's government. It may be fairly easy for the boss of a large Western multinational to see a senior state official, but for a Chinese citizen merely getting a few minutes with a lowly bureaucrat is an ordeal: he needs to fight his way past several offices, guards and indifferent assistants intended to keep him out.

And the local satraps are not that much more responsive to Beijing either. The central government has the clout to compel bureaucrats to act quickly on issues of national importance such as foreign investment or responding to emergencies like the SARS epidemic; but on plenty of other issues the local government ignores them.

For the clever young technocrats at the top, the medium-term prospects for the Chinese state must be quite frightening. The country needs to find a more secure way of financing local government. It must improve its current rudimentary health-care coverage, not least to cope with the ageing population that is the legacy of its one-child policy. Above all there are the demands of its increasingly affluent citizens. Most of them are well over half-way towards the income level of around $12,000 a year (at purchasing-power parity) which elsewhere in emerging Asia, notably Taiwan and South Korea, resulted in demands for greater political freedom and proper government services.

A long, hard march

During Wen Jiabao's much commented-on visit to Shenzhen last year when the city was celebrating its 30th anniversary as a special economic zone, he tried to alert his party to the perils of its position. "If there is no guarantee of reform of the political system," the prime minister said, "then results obtained from the reform of the economic system may be lost, and the goal of modernisation cannot be achieved."



By Chinese standards Shenzhen's "small government, big society" programme is fairly dramatic. The city has eliminated a third of its departments and scrapped a jobs-for-life pledge for newly hired bureaucrats; and through Ma Hong's office, it is trying to outsource work to NGOs. Sunny Lee, the founder of the Ciwei school, points out that until recently it would have been unthinkable for a non-party member like him to set up a school. He talks about Shenzhen being "an El Dorado for NGOs". Billboards around the city proclaim: "Civil Society: Grow Together".

But it is slow work. Although some departments have been amalgamated, the main bureaucrats have all kept their jobs, leading to an abundance of deputy directors (which also makes dealing with Beijing difficult). The structure is still complicated: technically only 40,000 people work for the city (teachers, for instance, are separate). Li Luoli of the China Society of Economic Reform points out that the local ministries and developers have been able to ignore Beijing because there is no specific local body behind political reform. A report on how to improve the local people's congress has been shelved, and talk of an anti-corruption commission has faded.

There is also a deeper cultural problem. Most reformers want to devolve power, but for a government that likes to control things this is hard to accept. The reformers have not been helped by the financial crisis. The failures of Western capitalism have put a spring in the step of the state-owned enterprises, and of state-directed capitalism in general. Shenzhen's reformers hail Hong Kong as a place where NGOs do a lot of the state's work, but most of Hong Kong's civil society is rooted in religion. The Chinese government is unlikely to let churches run schools; indeed, elsewhere in the country Catholic priests have been stopped from setting up networks of parishioners to check on old people, for fear that they might start proselytising.

China may aspire to the efficiency of Singapore and Hong Kong, but it is nervous about the idea of a small state. This hesitancy seems to go right to the top. Even though Mr Wen called on Shenzhen to lead the way to reform, Hu Jintao, China's president, who visited the city a couple of weeks later, did not reiterate the point.

The pressure from below will not go away. Mr Yang's office may have gone, but online forums now catalogue the country's bureaucratic disasters, even if they rarely name the guilty parties. Eventually the regime in Beijing will have to embrace government reform with the same gusto as economic reform under Deng.

Until then, whatever Davos man thinks, China will not provide many lessons in government for the rest of the world. If the West wants to improve the way it runs its affairs, it would do better to look to technology and management.

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The gods that have failed-so far

Could technology and good management bring the public-sector up to scratch?



ASKED to talk about how technology affects productivity, Peter Thiel, the venture capitalist who backed Facebook, draws a simple graph on his whiteboard: input on the Y axis, output on the X axis. He then dabs on two blobs. The private sector goes in the bottom right (you put in relatively little and get out a lot); government goes in the top left: a lot of input and very little output.

Mr Thiel, a prominent libertarian, may be unsympathetic to the public sector, but his chart is not a bad guide to the past 40 years or so. Productivity in government is difficult to measure and statisticians have generally stopped trying to come up with precise figures. But such numbers as there are all point in the same direction. With a few small exceptions, government lags behind the private sector.

Two closely related things have transformed the private sector since 1970. The more obvious one is technology: think what ATMs did for banking. But management ideas-everything from profit-related pay to lean manufacturing-have arguably done even more to raise productivity. Toyota spent less on computers and robots than General Motors did; it won by out-managing its rival.

The public sector has certainly dabbled in both these things. From Berlin to Bangkok, every big consultancy has a thriving public-sector practice. Many of the ghastliest examples of management-speak come from the public sector. And some of the biggest disasters in public spending have involved technology, such as the attempt to link up Britain's health records nationwide. But neither has really changed government profoundly.

The pessimistic explanation is that they never will: there are good reasons why the public sector will always be resistant to change. Optimists have to make the case that "this time will be different," which is harder. But just this once it could be true.

Government is different

Begin with the depressingly long list of reasons to be pessimistic. The most fundamental one remains the Baumol effect: labour-intensive services, such as nursing and teaching, have thus far proved as immune to productivity-enhancing technology as string quartets.

Another cause for pessimism is that government does not respond to normal pressures. Most obviously, there is rarely the threat of bankruptcy. Indeed, most of the examples of efficient government involve warfare or other crises.

The idea that business skills do not translate to politics would seem to be borne out by the string of businesspeople who have failed to make much of a mark in government. Silvio Berlusconi has achieved a lot less as Italy's prime minister than he did in business. A more successful transplant from the media industry, Michael Bloomberg, the mayor of New York, says he had not realised how different running a city would be: "People are motivated by different things and you face a much more intrusive press. You cannot pay good staff a lot of money...In business you experiment and you back the projects that win. The healthy bits get the money, and the unhealthy bits wither. In government the unhealthy bits get all the attention because they have the fiercest defenders."

There are even ideological reasons why liberals in particular should want to keep the state relatively inefficient. Joseph Nye, a former dean of Harvard's Kennedy School and author of a book on power, says that Americans do not really want their state to work too well: "There is something special about government. It has coercive power, so it is essential that you have a healthy scepticism of it."

So why should this time be different? The immediate reason is that in many countries the state is now so bloated that, even without changing the basic structure of government, it could be made much more efficient.

In the short term, assuming a recovering economy, government can surely be slimmed relatively painlessly-if only because it has grown so fat. The howls across Europe about unprecedented budget crises ignore three things. First, Sweden and Canada have chopped their public sectors after financial crises and lived to tell the tale (albeit against a much more clement global economic backdrop). Second, most European countries need do no more than reduce government spending to its level of three or four years ago. And third, many of the cuts are tiny by private-sector standards. At a private dinner in Paris recently a group of French businesspeople listened politely to a politician moaning about his department having to reduce its costs by 5%, until one of the private-sector bosses pointed out that he had knocked out a fifth of his costs in a little over two years. The politician shut up.

People can argue over the respective virtues of making across-the-board cuts or targeting particular departments (they usually do a bit of both), but managerially speaking it is not a tough ask. Reforming American defence procurement does not require structural change, just making use of the Pentagon's clout with suppliers. A recent study by the National Audit Office showed that Britain's National Health Service (NHS) could save pound500m (well over $800m) a year by bundling its buying power; there is no need for hospital trusts to buy 21 different forms of A4 file paper and 652 different kinds of surgical gloves.

In the longer term, though, two sorts of opportunities present themselves: changing what the state does; and changing its structure. The first set tends to be administratively (fairly) simple but politically hard. For instance, getting rid of industrial and agricultural subsidies makes sense, but politicians cling to them. Even bigger potential "quick wins", though ones fraught with political difficulty, are to be found in pensions. Switching state employees from defined-benefit to defined-contribution plans and raising their retirement ages to prevailing private-sector levels would save most governments a fortune-but not as much as upping the age at which everyone starts receiving their state pension.

When Bismarck introduced the world's first state pension system in 1889, he set the retirement age at 70, some 25 years beyond the average Prussian's life expectancy, so it did not cost much to run. When America brought in its Social Security system in 1935, average life expectancy was only 62. In the OECD countries men on average now live to 76 and women to 82. In most rich countries raising the pension age to, say, 70 by 2025, and thereafter linking it to life expectancy (which keeps on increasing), would go a long way towards reducing the government's structural deficit.

In America Social Security is known as the "third rail" of politics: state pensions electrocute any politician who touches them. But the case for increasing retirement ages is overwhelming. It also begins to open the door to a proper debate about social transfers, including things like means-tested benefits. That argument will be much easier to make if the second set of opportunities to do with updating the structure of the state has been grasped.

On this score, unlike on benefits and transfers, almost everyone agrees what needs to be done. Britain's Tony Blair puts it this way: "The modern Western state was created in the era of mass production and command and control, where governments told you what to do and provided everything. Modern life is about choice-and the state, even if it pays for something, should not be the only choice." He argues that creating "a post-bureaucratic state", with a small centre and a multitude of public and private providers, should be a particular cause for the centre-left to embrace. "In every other walk of life a citizen gets services from bodies that are anxious for their business. We have to open up the state to transparency and competition, or else anyone who is rich enough will pay to opt out."

Mr Blair has no truck with the idea that the public sector is bound to keep growing. The key, he thinks, lies in breaking the state down into innovative smaller units, like charter schools in America and academies in Britain. "As more and more choices are made by consumers, not politicians, we will shrink the state," he predicts.

As is his wont, Mr Blair tends to be more messianic about this than most politicians. But to see how such ideas might work, consider two changes in the car industry. First, in the era of mass production Ford did not just make its own steel; it also owned the fields on which grazed the sheep whose wool went into the covers of its car seats. Now it contracts out much of this, even though its name remains on the car. Second, in the 1970s there was a big gap between the quality of the output and the efficiency of, say, Japanese carmakers and their American peers. Now competition has minimised that advantage (and no longer always in favour of the Japanese).

Don't do it yourself

For its part, the public sector in many countries still wants to do everything itself. Surprisingly, America, the country that has preached the Washington consensus of privatisation to the world, still owns a lot of its railways, ports and water systems; it also makes less use of for-profit schools than does Sweden. And if Britain's gargantuan NHS were to contract out as much of its business as the French and Dutch health services do, it would be a lot more efficient. The District of Columbia has shown how much can be saved by outsourcing: it has reduced its e-mail costs by 80% and its video-hosting costs by 90% by moving them to Google and YouTube respectively.

The huge variance in performance between different bits of the public sector that do the same thing is shocking. Sweden spends half as much on health care per person as America does, yet Swedes live longer. Research on degree courses at public universities shows that some Western countries spend 30% above the average on a degree whereas others remain 70% below it, says Lenny Mendonca, a public-sector expert at McKinsey. "In anything even resembling a free market, many of the best-performing public institutions would have wiped out all the others," he adds.

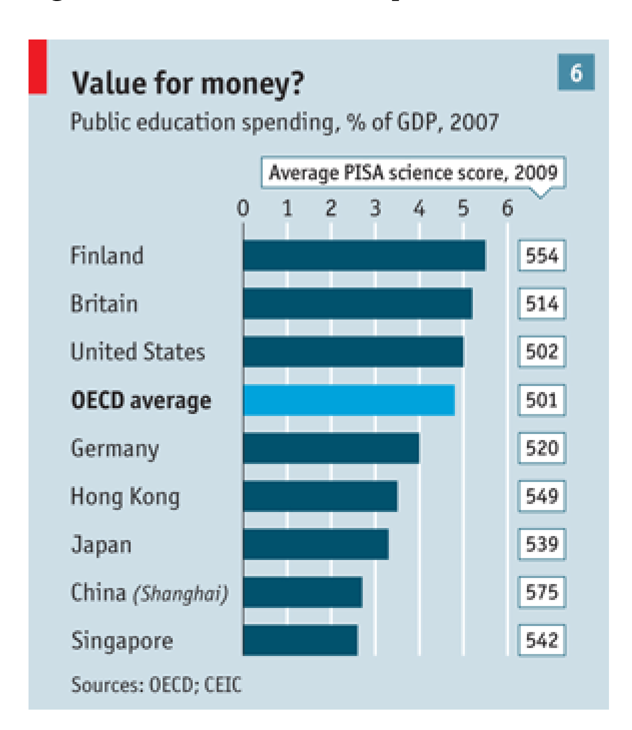
Variance within countries is harder for public-sector unions and other local vested interests to ignore. Sir John Oldham, an expert in health productivity, points to two similar adjacent areas in southern England where "unscheduled admissions" to hospitals (ie, the expensive sort) vary by a factor of eight; in another there is a 13-fold difference in the number of hospital referrals from similar doctors' practices.

By reducing these variances, quality would be improved and a huge amount of cash could be saved. Sir John has calculated that if every NHS organisation in Britain currently operating at costs one standard deviation above the mean were to improve its performance to the mean level, the NHS would save somewhere close to the pound15 billion it is supposed to find over the next five years.

It is about care as well as costs. The McKinsey Global Institute points out that at some American hospitals nurses spend under 40% of their time with patients. Naming and shaming is one way of getting better results. Sweden's health registries, a much-cited example, provide statistics on the performance of individual hospitals. The fear of coming out badly in a national league table is a powerful incentive to try harder. A study by the Boston Consulting Group found that Sweden's National Cataract Register not only reduced the severity of astigmatism resulting from eye surgery but also narrowed the variance between the best and worst hospitals by half.

Just wait till they find out

With such examples in mind, some argue that government reform will be akin to a popular revolution, driven by the spread of information. Just as American motorists, resigned to cars that broke down, rapidly ditched Detroit's products once they found they could buy cars that worked, so American parents will no longer tolerate the excuses of the teachers' unions when they discover that children get a much better and cheaper education elsewhere.



There is something in this. Few politicians now question the need to publish school-performance tables, despite the furious fusillades from the unions when they were introduced. One education minister argues that the most powerful force in school reform now is the OECD's international PISA ranking (see chart 6). "Waiting for Superman", a documentary by Davis Guggenheim, the director who made "An Inconvenient Truth", but this time attacking America's teachers' unions rather than climate-change deniers, was a big hit. As charter schools and the like outperform their peers, there is pressure to break up the old fiefs and introduce competition.

Clayton Christensen of the Harvard Business School, perhaps the world's most respected writer on innovation, thinks the public sector will be upset by what he calls "mutants"-new organisms spinning out of it. He points to the success of Guaranteach, an online store of teaching videos set up by two former teachers in 2008, and other similar outfits.

A new wave of frugal innovation coming from emerging markets will also make an impact on the public sector. South Korea is a leader in education testing. India is taking a dramatically different approach to health care. It has found a way to reduce the cost of heart operations by setting up huge hospitals that can reap economies of scale. It is already cheaper for Westerners to fly to India as health tourists than to have treatment at home.

Many think the web will shift the balance of power between the public sector and its clients. Worried about your child's school? You can join a discussion group on Facebook. Furious with the American government? You can see how much it is costing you at mygovcost.org. Fed up with Britain's lousy roads? Go to fixmystreet.org. Don Tapscott, one of the cleverer cybergurus and co-author of "Macrowikinomics", points to the rise of "prosumers": rather than merely accepting what the government offers, citizens will shape new services as they appear. Places like the District of Columbia and Canada's province of New Brunswick have been pioneers, spurred on by a new generation of younger, more web-savvy civil servants. Even health care-the field most resistant to change-could be turned upside down (see article).

So a bottom-up revolution is under way. But for all the obvious reasons, it is advancing more slowly than it did in the private sector. For instance, a recent survey by the *New York Times* of failed schools in eight American states that were bad enough to get federal turnaround money showed that 44% of the schools' principals had kept their jobs. Resources are another problem: there are fewer computers in the public sector than in the private because many government departments still do not distinguish capital budgets from operating ones.

Mr Christensen thinks one of the main problems is the lack of a common language. As a young academic he was able to persuade Intel to change course by telling its bosses that the sort of disruptive change that had happened in steel (the arrival of cheap mini-mills) would also happen in chipmaking. Yet when he goes to health-care conferences, he says, nobody uses the same terminology. Doctors, insurers, hospitals and politicians all talk about completely different things: "The only people who could really bang heads together would be the federal government."

Indeed, for all the evidence of mounting pressure from below, a command-and-control organisation will change only when the top wants it to do so. And here most Western countries have something in common with China: leaders are scared. Some attempts to institutionalise innovation have been made. Geoff Mulgan points out that America has committed $650m to a schools-innovation fund; Britain has allocated pound200m to health. Barack Obama has appointed Vivek Kundra, the man who led the District of Columbia's technology drive, as America's first chief information officer. Mr Kundra has already saved $3 billion by culling programmes.

Yet the same Mr Obama has recently delivered a budget to Congress that does nothing to reform entitlements. It is not just the threats from vested interests that inhibit progress. Mr Mulgan explains that the first wave of privatising governments in the 1980s and 1990s often did badly at the ballot box. Voters could not see enough change to justify the aggravation. And sometimes restructuring was done in several phases, so it was not clear who was responsible for the good things.

The recent economic crisis has changed minds. There now seems to be far greater acceptance that government is broken, and voters are more prepared to give their leaders leeway to mend it. Even if the debate has barely begun to tackle benefits and social transfers, that still gives politicians an opportunity. In various American states governors have seized it. But on a national scale nobody has grabbed it with more gusto than an Old Etonian Tory.

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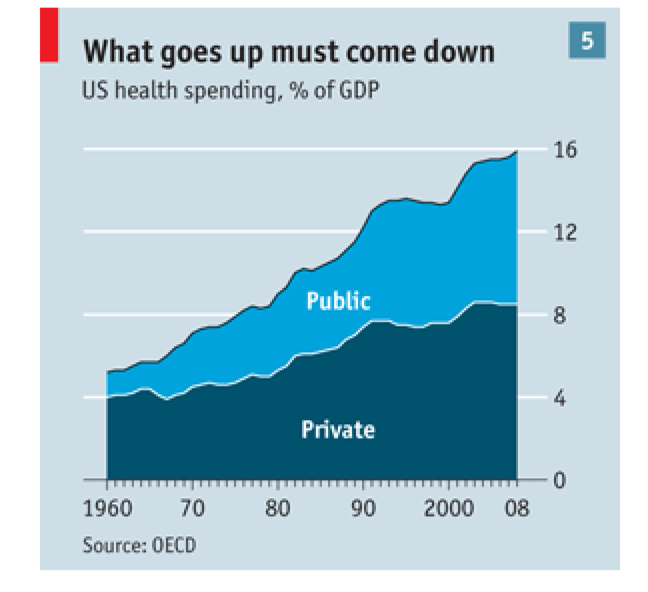
A special report on the future of the state

Patient, heal thyself

A bottom-up approach to the biggest problem in government

IN ANY discussion about the role of the state, one subject soon dwarfs all others: health care. McKinsey points out that American spending on this has grown at an annual lick of 4.9% over the past 40 years, whereas GDP per person has grown by just 2.1%. Pessimists are convinced nothing can be done to restrain it. A refreshingly different perspective is provided by Sir John Oldham, a British doctor who is clinical lead for productivity in the National Health Service.

His view of what he calls the coming tsunami is as pessimistic as anybody's. Health costs, he points out, are determined by long-term conditions-things like diabetes, heart disease, obesity and lung disease, which are usually linked to lifestyle and diet. Some 15m Britons suffer from such conditions, which take up 70% of "bed days" in hospitals.



The numbers of cases in other countries are equally worrying. They explain why America, which currently spends 16% of its GDP on health care (see chart 5), is theoretically on track to spend 100% of its GDP on health care by 2065, followed soon by Japan. China too has seen a huge rise in such conditions. They are no longer diseases of the old: in America, says Sir John, the Facebook generation is picking them up so rapidly that it might be the first not to live longer than its parents. But they are still mainly diseases of the poor, who live less healthy lives, smoking more, drinking more and consuming more salt and trans fats in processed food.

A hard-hearted economist might spot potential savings (especially on pensions) from people dying younger. But even he would be disappointed: any such savings would be wiped out by the adverse effect of such diseases on the productivity of the working-age population. One obvious way to alleviate this problem is to tax the things that are causing it: when governments are having to strengthen their ambulances to cope with heavier patients, it is time for a levy on cheeseburgers. But Sir John reckons that getting patients to help manage their illnesses might be even more promising.

Technology is starting to make this vastly easier. Futurists dream of small gadgets roaming people's bodies and reporting their findings to computers, but lower-tech versions of this already exist. In one pilot scheme in Britain's Stoke-on-Trent patients use fairly basic methods to record their own weight, cholesterol, blood pressure and so on every week and text the result to a computer, which tells them what to do about them.

This can be economically attractive, because the most expensive things in health care tend to be unscheduled visits to hospital. But it also improves people's health. A patient is always around to monitor himself, and he will be highly motivated. A big study by the Cochrane Institute showed that among people who managed their own anticoagulant treatment, repeat blood clots declined by half; deaths from clots also fell.

Sir John suggests that the NHS should set up an incentive scheme for its workers to lead healthier lives that would create rewards (or, as he likes to call them, "care miles"). That would set a good example. But for the biggest employer in the country it could also save a lot of money.

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Big society

Radical ideas from a fusty old island



FOR all its pomp and tradition, Britain has played an outsized role in promoting radical thought about the state. In the 19th century it championed modernisation, with the same liberal Victorians who campaigned for free trade (and set up this newspaper) also dismantling the courtly system under which posts in government were sold off or given to political allies. The Northcote-Trevelyan report of 1854 led to the creation of a politically neutral civil service, with appointments made on merit. Liberals prided themselves on the leanness of a state that ruled India with a few thousand bureaucrats. John Stuart Mill, himself a civil servant, famously defined this minimalism: "The only purpose for which power can be rightfully exercised over any member of a civilised community, against his will, is to prevent harm to others. His own good, either physical or moral, is not a sufficient warrant."

Yet as the 19th century wore on, "New Liberals", including Mill himself, began to question the morality of the "night-watchman state". How could liberty flourish when so many people lived in misery and ignorance? Reforming governments introduced compulsory education, laws to regulate safety at work, tax-funded libraries and welfare-all robustly condemned by Herbert Spencer in his libertarian bible, "The Man versus the State" (1884). But the intellectual traffic was mainly towards more intervention, with socialists (Karl Marx and Friedrich Engels were based in London) and then Fabians taking New Liberal arguments to the extreme. A more active state became the answer.

Britain continued in that vein for most of the 20th century, with the Depression only increasing anti-market sentiment. In 1938 an ambitious young right-wing MP surveyed the British economy: "The weakness of partial planning seems to me to arise from the incomplete and limited application of the principles of planning. The lesson of these errors, which I regard as errors of limitation, is not that we should retreat. On the contrary, we must advance, more rapidly and still further, upon the road of conscious regulation." Harold Macmillan went on to become a post-war Conservative prime minister, which shows how far the centre had shifted.

Gradually, however, an anti-state right began to emerge. In 1960 Friedrich Hayek wrote "The Constitution of Liberty", partly in response to what he saw in Britain. In 1978 another young Tory with a Macmillanish pedigree, William Waldegrave, took a very different line in "The Binding of Leviathan": "No one knows how to run bureaucracies. Bureaucracies are increasing. No wonder the public thinks something is wrong." In 1979 Margaret Thatcher hurled herself at these bureaucracies-and a new creed, very different from Fabianism, rippled out across the world.

Now the promise of renewed radicalism is in the air. David Cameron's coalition government of Conservatives and Liberal Democrats is pursuing the most daring course in the rich world. That judgment is based on two things: the severity of its spending cuts (many departments are being slimmed by a fifth) and the fact that it is trying to change the structure of the state.

The spending cuts currently dominate the British media. Manchester is in turmoil because it will be reduced to only one public lavatory. The Tories are plainly taking an economic gamble by tightening fiscal policy so fast, but seem less fixated on the overall size of the state than Mrs Thatcher was. For political reasons they left health care, perhaps the most wasteful part of the British state, out of the cuts. One senior Tory thinks you cannot reduce state spending below around 40% of GDP, or the politics will turn against you.

The bolder reforms, championed by Mr Cameron's main domestic adviser, Steve Hilton, are centred on structure. They are hidden behind a confusing slogan that the Tories adopted to make themselves sound cuddlier: "The Big Society". It brings together three things: pluralism, localism and voluntarism.

How to get there

To promote pluralism, the Tories aim to build the "post-bureaucratic state" that Tony Blair wanted (they even use the same phrase). Haunted by the idea that Mr Blair did not move fast enough, they are rushing to hand over many more state services to outside providers. They have opened the doors to Swedish-style free schools set up by parents, and they want more parts of welfare to be delivered by outsiders, paid by results. They have also announced the biggest shake-up in the history of the health service by shifting spending power to groups of general practitioners, who will buy in services from both public and private hospitals.

Haste has caused problems. Whereas the education reforms follow on neatly from the academies that Mr Blair set up, the changes in the health service, introduced with little prior warning, come just as the system is adapting to the previous round of reforms. Oddly for a party that believes in the free market, the Tories have rejected for-profit providers for some services, notably education.

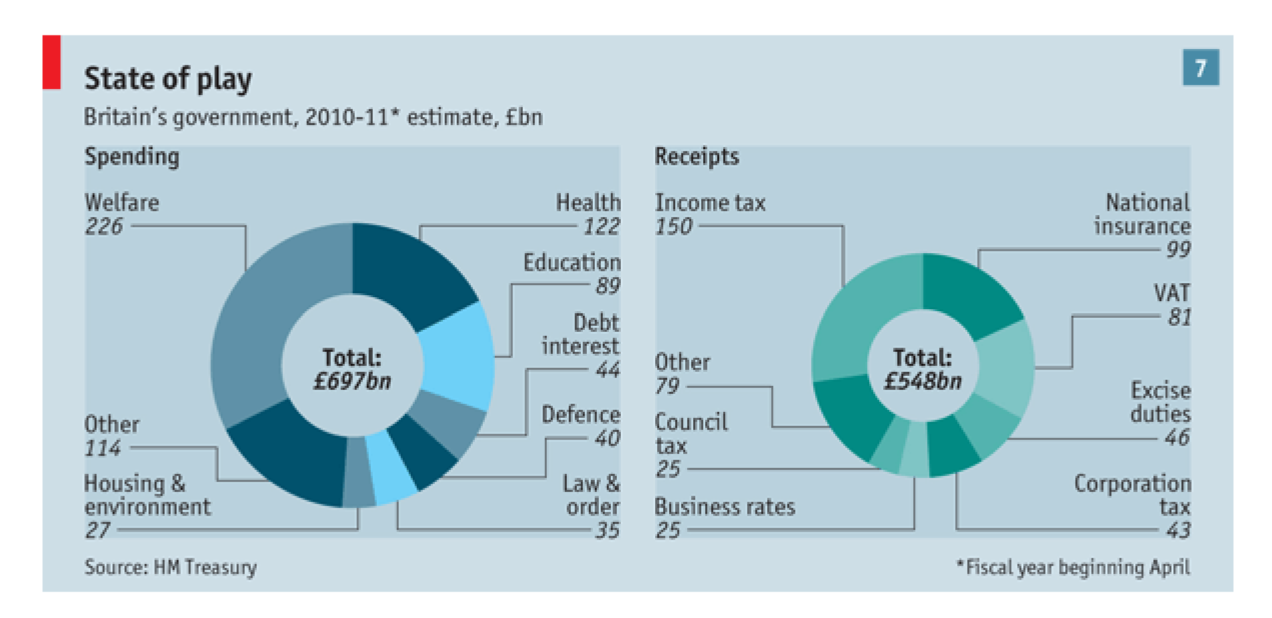
Even so, pluralism could lead to a much smaller civil service than anyone thinks. "Once you start letting people compete, it is incredible how few people you need in the centre," says one of Britain's most senior mandarins. And, since the change is technocratic not political (the state, after all, is still paying), it will be difficult for a future Labour government to reverse.

Handing over control of schools to parents and medicine to local doctors also fits in with localism. The Tories want more cities to have elected police chiefs and, eventually, elected mayors, like London's Boris Johnson. They are providing reams of information to make government more transparent; a new crime map of Britain's streets crashed on its launch day because so many people wanted to see it. Combined with pluralism, this amounts to a substantial attack on the centralised state. For instance, Suffolk County Council hopes to knock a third off its budget of pound500m by becoming a "virtual" authority that outsources all but a handful of its services to social enterprises or companies.

This localism is somewhat marred by the Tories' deep distrust of local government. Handing over schools to local associations risks creating bodies that can be taken over by teachers' unions, as in America. Lord Adonis, a Blairite who now heads the Institute for Government, a think-tank, argues that the Tories should also have given more power to elected local mayors, especially in the 14 big cities where one in three Britons live. Apparently Tory and Liberal-Democrat local councillors took against this.

Volunteer, or else

Volunteerism, the idea of Burkean small platoons taking on the functions of the state, is the trickiest part. On paper, this is a big idea. The people around Mr Cameron argue that just reducing the supply of government won't wean people off the state; you also have to reduce the demand for it. That persistent demand, after all, has been the main reason for sprawling government from California to Cardiff.



In practice, however, the idea has flaws. Running your local library sounds attractive, but most people lack the time and expertise required, and there is not a lot of money around to help them (thanks to the spending cuts). Britons seem to band together of their own accord only when they want to oppose something-such as the government's plans to sell off the nation's forests, which they halted.

To be fair to the Tories, the Big Society is not their only scheme to reduce demand for government. Their welfare reforms are based on moving poorer Britons away from dependence on the state. A lot of state spending is "avoidable", argues one insider: if you can get people into jobs, strengthen families, stop teenagers getting pregnant and teach children early, you will save a fortune a decade hence. Just two particularly troublesome families have cost British taxpayers pound37m over three generations.

The Cameroonians are also trying to do something about the tangle of regulation that costs the British economy around 10-12% of GDP. A neat scheme whereby any new rule would have to show a net decrease in regulation was shelved after civil servants gamed the system. One of Mr Cameron's advisers, Oliver Letwin, is now working on another plan. But not all the regulation is domestic. A British Chambers of Commerce study of 144 new rules in 1998-2010 put the total cost at pound88 billion, of which two-thirds was attributable to European Union legislation.

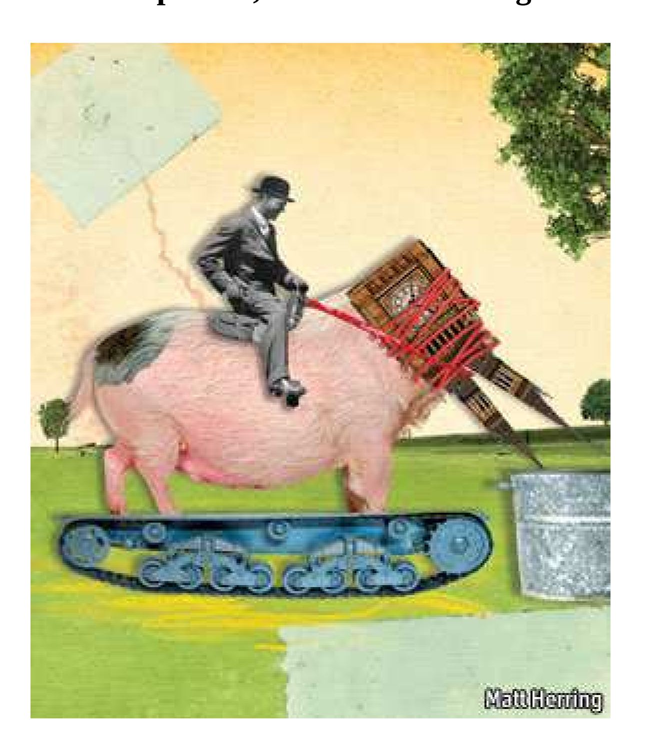
Implementation is crucial: unless reform of the state is seen to be equitable and effective, citizens will not accept it. But with that huge caveat, two things stand out. First, the government's breadth of ambition is impressive-even set against that of Mrs Thatcher, who did far less in her first year. And second, most other rich-world governments will have to do something similar soon. That is partly because of their fiscal situation: even America will have to start reconciling its revenues and its spending in the near future. And once you start to cut, you need to decide what should go and what should remain. Mr Cameron, for all his haste, is at the front of a great wave. In that, he resembles Mrs Thatcher-and those great reformers of the 19th century.

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Seize the moment

The prospects for reforming the state have improved, but it will be a long haul



HOW far and how fast could reform of the state go? For now that question seems fanciful, like asking how a man who has been getting fatter for decades would do in a marathon. Yet fatalism about an unreformable state seems misguided.

To begin with, the patient is not in his current condition by design. In a forthcoming book about the role of the state, Vito Tanzi, an Italian-born economist, shows that it changed dramatically during the 20th century. Demands on it grew continuously, and theories of what it might capably do expanded to meet those demands. What began as a "normative" state, designed to offset market failures and help the poor, broadened immensely to become an active redistributor of wealth and creator of universal public goods, hoovered up by the middle class in particular.

"If something cannot go on for ever", Herb Stein once pointed out, "it will stop." There are several reasons to think that some time soon-maybe next year, maybe later this decade-the seemingly endless expansion of the state will begin to go into reverse. One is the political pressure from deficits. The shape of the state could be the main issue in America's presidential election next year. Even left-wing governments are increasingly looking at the spending side of the ledger.

Globalisation is another. Commerce has proved stickier than the proponents of borderless capitalism proclaimed in the 1990s, but it is less sticky than it was. The mobility of talent, technology and capital surely puts some limit on governments' ability to keep on raising taxes. Government is becoming a more competitive business, not just in terms of lower spending but also in what it offers for the money.

Above all, the incremental benefits of ever bigger government, even assuming it was somehow affordable, become ever smaller. Decent-sized government can reduce inequality and poverty, but most of the evidence is that gargantuan government merely gets in the way of social progress. A state that takes up more than half the economy begins to deliver an ever worse deal to ever more people in the middle: the extra benefits become harder to detect, the extra costs harder to hide.

Guessing when this penny will eventually drop is a little like speculating when an investment bubble will burst or a dictator will fall. There are always reasons for delay but, once things begin to move, they do so quickly. A revolution in government would come in three stages.

The first, which this special report has concentrated on, might simply be described as good management. Purely by copying what other countries (or bits of their own system) do well, governments could save a huge amount of money. The path forward is pretty clear-towards a small central state buying in services from a variety of different providers. Technology could speed things up. A huge quantity of information about just how poorly bits of government are doing is becoming available-and, thanks to Facebook and other new media, shareable. Transparency will also affect demand. Too many voters are "Californians": they think they can enjoy ever more services without paying for them. When they see the true cost of government, they may change their minds.

Within the public sector, mayors and senior civil servants could play a pre-eminent role. Not only do many public services, such as education and the police, work best at city level; cities are natural test-tubes for experimentation. In the urban West, mayors can still change things visibly: think of what Rudy Giuliani did for crime in New York. As for senior civil servants, most feel despised, underpaid and deeply frustrated. More than anybody else, they stand to gain from a world where government works.

Good management sounds a little worthy, but it could achieve a lot. Imagine, for instance, that Mr Cameron succeeds in creating a "post-bureaucratic" state in Britain. You might end up with a government that delivered the same range of services-defence, justice, education, health care and so on-but consumed perhaps 40% of GDP, roughly ten points less than it does now.

Could it go further? The second stage is more difficult: limiting the scope of those services, especially the universal benefits enjoyed by most Western voters. Social transfers have accounted for a large part of the growth in the state: they also explain why even a well-run version of Britain's all-you-can-eat "buffet" state would be twice the size of Singapore's. Unless Western governments start to reform entitlements, the state will swell again in line with their ageing populations.

Some universal benefits can be trimmed across the board. State pension ages, for instance, are on the rise. But governments also need to start redirecting social programmes at the truly needy.

Persuading middle-class voters to give up their perks will be extremely hard. One possible avenue is to hand them greater control over their own benefits, perhaps by switching pay-as-you-go systems to individual savings accounts (like Singapore's Central Provident Fund). That has not had much success yet-in part because most people, especially the young, are in the dark about how much the current system is really costing them. Tax simplification would help. A bipartisan commission on fiscal reform last year said that if the American government abolished all tax breaks (including middle-

class ones like mortgage-interest relief), it could reduce the top individual tax rate from 35% to 23% and still generate $80 billion more revenue. Again, limiting benefits will be a colossal struggle.

Rules not OK

The final stage-untangling the web of rules-would on the face of it be less controversial. Everybody agrees that there are too many regulations. But in practice it could be the most fiddly to sort out. The European Parliament does not cost much to run, but it litters the continent with expensive rules. One in five American workers needs a licence to do his job. Sunset clauses to make laws expire in the absence of political reapproval would help.

This special report has tried to be pragmatic, focusing on what works. At the moment it is hard to see that society would gain much from even larger government, and easy to spot the gains in productivity, efficiency and personal freedom that would come from smaller government. States exist not only to lead society towards common goals; they must also provide people with the liberty to live their own lives. Over the past century government has moved too far towards the former. Now is the time to turn the dial back. Nothing would add more to the sum of human happiness in the West than a smaller, better state.

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Sources and acknowledgments

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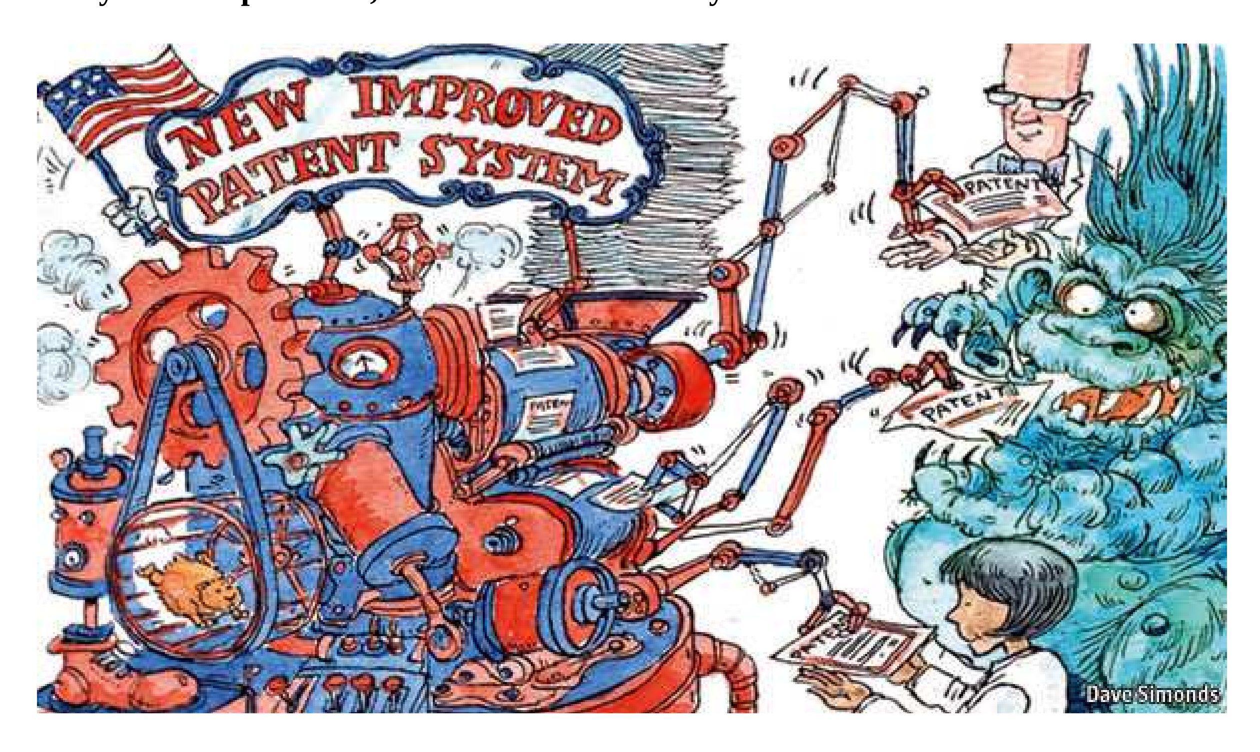
Offer to readers

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Patent reform

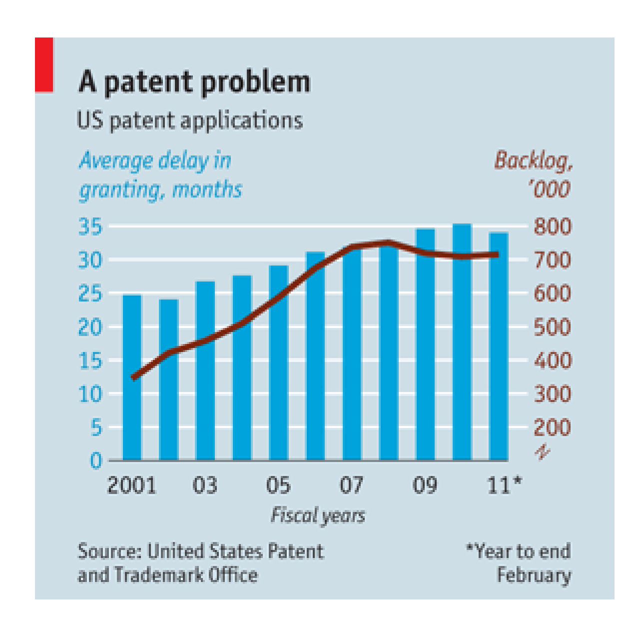
The spluttering invention machine

America's patent system has problems; a new law would fix only a few



FOR all America's anxieties about its decline as a superpower, its deficits and its weak economy, it can still be proud of its strength as an innovator. Americans make four times as many patent applications per head as Europeans. Patents spur innovation and lay the foundations for future growth, by assuring inventors that they will reap the rewards of their effort and by publicising their discoveries.

But worries have grown that excessive patenting may now be having the opposite effect: businesses and other researchers may be discouraged from innovating in areas that depend heavily on prior discoveries, for fear of being sued for patent infringement. Besides making it too easy to bring patent lawsuits, it is argued, America hands out patents too readily: an often-quoted example is the one granted to Amazon for its "one-click" online-shopping button. Last year the Supreme Court restricted the scope of such business-process patents, but not by enough to satisfy critics.



Big technology companies complain of "patent trolls"-companies that buy lots of obscure patents and then bombard alleged infringers with lawsuits. (The "trolls" argue that by making patents valued they are helping to create a market in invention that will encourage inventors.) Surging patent activity has overwhelmed the US Patent Office, which is taking ever longer to process applications (see chart).

After years of failed attempts to remedy the situation, on March 8th the Senate passed the biggest overhaul to patent law since the 1950s. Its bill would give the patent office the right to set its own fees, and keep all the proceeds (the Treasury swipes some of these now), so it can hire enough examiners to cut its backlog. It would also align America with international practice by granting patents to the first person to file them. Now, they are awarded to the first to invent a product or idea. This was intended to give small inventors a fair chance against big companies better equipped to file

applications. But businesses complain about having their patents challenged, years after they were granted, by people claiming to be the original inventor.

Barack Obama, who includes patent reform in his grand campaign to make America more competitive, has praised the bill. It now has to pass in the House. But even if it becomes law it will not please all the many businesses and other organisations that file patents. Some think it will still be too easy and potentially lucrative to bring lawsuits for patent infringement. Others wanted it to be made easier to challenge patents. Josh Lerner, an economist at Harvard Business School, faults the bill for not giving third parties a means to object to a patent before it is granted. It does create a process for opposing a patent afterwards, as in Europe, but some say it will still be too burdensome for the challenger. Those hoping for a broader crackdown on business-process patents will also be disappointed.

Europe is seeking to improve its patents system, too. On March 9th finance ministers from 25 of the 27 European Union countries agreed to the creation of a single European patent which would not need separate validation at national level-which has been a glaring gap in the single European market. (Spain and Italy for years did their best to block it because patents would have to be translated only into English, German and French.) The plan must now be approved by the European Parliament. Bruno van Pottelsberghe, an intellectual-property expert at Solvay Brussels School of Economics and Management, says this will slash the cost of a European patent to just a few times the cost in America; it now costs about 15 times as much. Even so, he complains that national patent offices will still issue patents independently, which may undermine the value of those of the European Patent Office.

A unitary patent will not make Europe a hotbed of innovation. But it will help. And despite the flaws in the new laws, the attention to patent reform on both sides of the Atlantic is good news for business.

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Mexico's communications monopolies

Amigos no longer

Billionaires feud over converging television and telecoms markets



What's on television tonight? Nada, as usual

MEXICO'S telephone and television industries are near-monopolies. About 80% of landlines are connected to Telmex, one of many companies controlled by Carlos Slim, the world's richest man. Another of Mr Slim's firms, Telcel, has 70% of the mobile-phone market. A second-division billionaire, Emilio Azcarraga, maintains almost as tight a grip on the

television business, in which his company, Televisa, claims 70% of the country's free-to-air TV audience. Most other viewers are mopped up by TV Azteca, run by Ricardo Salinas, the country's fourth-richest tycoon.

The Mexican billionaires' club has long been cosy. Apart from some sporting rivalry between the two broadcasters, there has been little reason for members to intrude on each other's captive markets. Until now. On March 9th a group of 25 companies led by Televisa and TV Azteca filed a complaint with the competition authorities against Mr Slim's telephone empire. Full-page newspaper ads denounced the industry's "expensive and bad monopoly".

The same day Mr Slim filed a complaint of his own, accusing the television moguls of conspiring to block him from the TV business. Already in February he had withdrawn advertising worth $70m a year from Televisa's channels; the same month, Mr Salinas forbade Mr Slim from advertising on TV Azteca.

What has prompted the three amigos' bust-up is the convergence of their fiefs. Technology has made a single market of the phone and television businesses: Televisa now bundles phone and internet with its cable-TV services, and wants to add mobile phones. Mr Salinas, who also controls a cellphone company, Iusacell, launched a similar package last year. Mr Slim longs to use his phone cables to distribute pay-television (in which he has become the biggest player in the rest of Latin America), but the government won't allow it.

The billionaires are now calling for just the sort of competition reforms that their respective industries have long needed. The TV moguls want Mr Slim to cut the amount charged when a rival phone calls a Telcel mobile (this week Mexico's telecoms regulator told it to cut some such fees). The current interconnection rate is 43.5% higher than the average in the mostly rich-country OECD; this makes it impossible for other operators to offer competitive tariffs. Mexico's Federal Competition Commission (CFC) says consumers would benefit by $6 billion a year if connection charges matched the OECD average. The CFC recommends letting Mr Slim compete in television once he has relaxed his hold on the phone business. If Telmex were to enter the pay-TV market, the increased competition would bring prices within reach of a further 3.8m homes, the CFC reckons.

The Mexican government has shelved such proposals for years, anxious not to upset the powerful interests involved. With a presidential election next year, it is on timid form. But now that the TV and phone giants are each demanding concessions of the other, it may be possible to broker a deal. This is the best opportunity for reform in five years, one CFC official believes. The danger is that the billionaires think twice, and realise they are better off sticking with their cosy near-monopolies than competing against each other.

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Online-coupon firms

Groupon anxiety

The online-coupon firm will have to move fast to retain its impressive lead



GROUPON has arrived in China. On March 16th the online-coupon firm's new site there-a joint venture with Tencent, the country's biggest internet company-began offering daily deals such as 75% off the regular price of a trip to an indoor hot-springs resort. Initial signs were that Chinese consumers will rush to snap up Groupon's offers, as they have in many other parts of the world.

In 2009 Groupon was a virtual nobody, confined to just 30 American cities, with 120 employees, 2m subscribers and just $33m in revenues. By the end of 2010 it had become a global success, with more than 4,000 staff, 51m subscribers in 565 cities worldwide and $760m in revenues.

Yet amid all the excitement over the "world's fastest-growing company ever", as some have breathlessly described Groupon, words of caution can increasingly be heard. Even Andrew Mason, the firm's habitually cheerful boss, seems to harbour doubts. "By this time next year, we will either be on our way to becoming one of the great technology brands", he recently wrote in an internal memo, "or a cool idea by people who were out-executed and out-innovated by others." More fundamentally, the whole idea of "daily deals" may have serious flaws.

The basic idea is nothing new. Consumers sign up to receive offers from local firms by e-mail each day, ranging from restaurant meals to pole-dancing lessons, at discounts of up to 90%. But Groupon made virtual coupon-clipping exciting by, first, having offers expire after just a few hours and, second, cancelling them if they do not attract a minimum number of buyers (the "group" in Groupon). Although this rarely happens, it induces buyers to spread the word among friends and family, boosting the uptake.

The daily frenzy has already spawned new phrases, such as "Groupon anxiety"-"the preoccupation and feeling of anxiousness and not being able to sleep knowing that a new Groupon will be released after 1am", according to The Urban Dictionary, a website which tracks such coinages.

Unlike lightly staffed but equally hyped internet firms such as Facebook and Twitter, Groupon needs an army of salespeople to negotiate deals with local businesses in each city it covers, and a further platoon of bright young copywriters to churn out the witty, whimsical e-mail pitches it sends out to consumers.

What makes Groupon really stand out, however, are its margins. It typically charges businesses half of the discounted price of a voucher. Venture capitalists say they have never seen such impressive numbers. This goes a long way towards explaining why the start-up was able to raise a whopping $1.1 billion in financing and why, in December, Google was willing to pay an even more astounding $6 billion for it.

Mr Mason walked away from the deal and has started the process of getting a public listing. This decision may come to haunt him. Groupon's position is not as unassailable as it appears from its rapid growth and huge market share-more than 60% in America, according to neXtup Research, which analyses tech firms. To ward off competition, neXtup reckons, Groupon will be forced to lower the share of revenue it keeps from its deals.

Deals a dime a dozen

For starters, almost anyone can set up a daily-deals site. And many already have. There are hundreds of clones in America alone, most specialising in certain product categories. To help overwhelmed consumers, there is even a service, The Dealmap, which lists all the daily deals available in a city. More dangerously for Groupon, big online firms have begun to enter the fray. In December Amazon invested $175m in LivingSocial, the market's number two, which is said to be in talks to raise a further $500m. And Facebook, the world's biggest social network, will soon start testing local discounts.

In addition, Groupon cannot rely on the "network effects" that have given companies such as Facebook and eBay, the world's biggest online-auction site, an almost unassailable lead: the more users such services have, the more valuable they become, thus attracting even more users. In the case of Groupon the network effects are comparatively weak. Being the biggest kid on the block is certainly an advantage: a long mailing list attracts better merchants, which pull in more consumers. But both businesses and consumers can easily switch to other sites.

Groupon's managers are aware of all this. Rob Solomon, its chief operating officer, agrees that the barriers to entering the daily-deals market are low and the network effects weak. However, he believes that, with the right strategy, the company can create competitive barriers to shore up its dominant position. One way it is doing so is to make better use of all the data it collects, for instance to personalise deals and help local businesses design their Groupon offers. Last year the firm hired as chief data officer an executive from Netflix, a film-rental business noted for its data-mining skills. In America Groupon already tailors some offers depending on the sex, location and buying history of a subscriber.

The next step is for Groupon to become a broader "platform for local commerce", in the words of Mr Solomon-a bundle of services that make that market more efficient. In America it has already started testing virtual storefronts where a city's businesses can organise their own deals. It is said to be working on a smartphone application that alerts consumers to a local business's special offers whenever they walk past its real-life storefront.

Besides having to keep one step ahead of its many competitors, there is another reason why Groupon needs to grow into a broader local-commerce operation: the daily-deals phenomenon, despite its remarkable recent growth, may have its limits. Although Mr Solomon claims that 95% of local firms using Groupon come back for more, independent research comes up with markedly less impressive numbers. Last summer Utpal Dholakia of Rice University interviewed 150 businesses that had done Groupon promotions. One-third said they did not make any money from them, and 42% said that they would not do another daily deal.

The reasons for such numbers are various. Businesses grumble that the deals attract mainly bargain-hunters who do not spend more than the coupon's face value and do not become repeat customers. Although these problems may be fixed by designing the promotions better, there are some longer-term worries. Studies have repeatedly shown that price discounts erode brand value, says Mr Dholakia. They may be good for giving businesses some exposure but the benefit of this is likely to wear off after a few such promotions. Mr Solomon will have none of this, calling Mr Dholakia's survey unrepresentative and insisting that Groupon has a queue of new companies keen to sign up.

Even so, there is a risk that local businesses, having given Groupon a try, will abandon it. How the behaviour of consumers will evolve is harder to predict. So far the hunger for online coupons seems insatiable. Groupon's best customers are young, female city-dwellers, who tend to be avid followers of fashion; but fashions change. Mr Dholakia has already seen signs of what the Urban Dictionary will probably call "Groupon fatigue".

Does this mean that Groupon will go the way of Napster, Friendster or MySpace, all of which had meteoric rises before crashing and burning? This is clearly a risk. But with its powerful momentum, strong management and hefty financial backing, the firm certainly has a chance of becoming the dominant platform for local service businesses to pull in the punters, much as Amazon has come to dominate online shopping for all sorts of physical goods. If so, though, daily deals will probably be just one of Groupon's offerings.

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Sports newspapers

Pink, and read all over

General newspapers can learn from the success of sporting dailies

FOR old-fashioned newspapers, the bad headlines keep coming. The Pew Research Centre, a think-tank in Washington, DC, reported this week that more Americans now get their news from the internet than from newspapers. But there is one sort of news that readers do still want to read on paper: a blow-by-blow account of a game involving their favourite sports team. Sporting publications' resilience explains why Innovation, a consultancy, is working on the launch of one new sports newspaper in Europe and the relaunch of another with a heavy emphasis on sport.



La Gazzetta dello Sport, a fixture of Italy's bars and football stands, recently recorded an average daily print readership of 4.3m-a record for any newspaper in the country. Spain's four biggest sports dailies, helped by the national team's triumph at the FIFA World Cup, have been doing far better than its top general newspapers (see chart). Many of their readers are newspaper-allergic young men.

Online audiences can be much bigger. Last year *Marca*'s website had 27m unique visitors a month, a colossal tally for a Spanish outfit. One-third of its total ad revenues come from the website, a remarkably high share. Other sports papers have gone into e-commerce and paid news delivered via mobile phones and tablet computers.

One reason for their success has to do with the peculiar nature of sports-media consumption. Three years ago ESPN, a TV sports giant, commissioned a study in which American sports fans were followed around by researchers. They found fans consumed about twice as much media in an average day as other young men. They watched more television, listened more to the radio, checked for news on their mobile phones more often-and spent more time reading newspapers. Often, the growth of one news source comes at the expense of another. In sport that is not always the case.

There are a few national sports papers, like *La Gazzetta dello Sport* and France's *L'Equipe*. But most are local, and deeply tribal. *Tuttosport*, based in Turin, is described by one Italian journalist as "the *Pravda* of Juventus", Turin's top football team. All sell better when the local team wins. Yet even the most partisan papers can be brutal in their treatment of underperforming players and managers. They serve the fans, not the teams.



Mamma mia! Lazio lost again

The sports papers are not entirely immune to the broader news business's problems. The paid circulation of many of them is slipping even as their readership grows. Nicola Speroni of *La Gazzetta dello Sport* points to competition from fan websites, satellite television and general newspapers, which are devoting more space to sport. But sports newspapers have two advantages. First, they are less fussy about separating news from advertising than most publications. *Marca* has gone so far as to change the letter "M" in its headlines to resemble the logo of Movistar, a mobile-phone firm. Second, they tend to treat their readers better. *Gazeta Sporturilor*, a Romanian paper, recently began creating what it calls "wikis"-articles incorporating readers' comments and suggestions.

Sports newspapers hardly exist in English-speaking countries, and seem unlikely to appear. In Britain, tabloid and even broadsheet newspapers monopolise coverage of sport. In America fans are spread between too many different sports, and the population is too mobile, to support local sports newspapers. An effort to launch a national one collapsed in 1991.

But other publishers could nonetheless learn from the sports papers, argues Juan SeÃ±or of Innovation. The internet has not so much made paper obsolete as broken the model of aggregating news on paper. Consumers are moving away from bundles of domestic, national and international news, opinion, weather reports and TV listings. The papers that survive may be the ones that deliver one kind of news extremely well. The sports newspapers have done that since the starting whistle.

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Online privacy

Stopped in their tracks

A proposed privacy law could help as well as hurt America's web companies

THE outcry over internet firms' habit of surreptitiously tracking web surfers' activities has clearly resonated inside the White House. On March 16th the Obama administration announced that it intends to work with Congress to produce "a privacy bill of rights" giving American consumers greater control over how their information is collected and used by digital marketers.

Those who have been lobbying for change agree with, but are unsympathetic to, internet firms' worries that such a law could dent their advertising-driven business models, which rely on tracking and targeting consumers to maximise revenues. "This is dimming the prospects of Google, Facebook and other digital ad companies," says Jeffrey Chester of the Centre for Digital Democracy.

Quite how dark things get for them will depend on the details of the bill. It will seek to lay down the basic principles of internet privacy rights, broadly following recommendations published last December by the Department of Commerce. The department's report said consumers should be told more about why data are being collected about them and how they are used; and it called for stricter limits on what companies can do with information they collect.

Whatever legislation finally emerges is likely to give a broader role to the Federal Trade Commission (FTC), which will almost certainly be charged with deciding how those principles are translated into practice and with policing their implementation. Among other things, the FTC is known to be keen on a formal "do not track" system, which would allow users to block certain sites from monitoring their online activities.

Keen to avoid this, the online-advertising industry has been working overtime to convince policymakers that it can police itself using systems such as icons on web pages that show surfers when they are being tracked. And it is telling anyone who will listen that consumers will suffer if tough do-not-track rules hit ad revenues, forcing web firms to charge for more content.

With Mr Obama throwing his weight behind internet privacy, this rearguard action is less likely to be successful. Some ad firms have started talking of creating a do-not-track system of their own, that would limit the damage to their digital activities. Microsoft and Mozilla, two tech giants, have recently said they are including do-not-track features in new versions of their respective web browsers, Internet Explorer and Firefox.

Although all this may dent their revenues, America's internet giants could also benefit from the legislation if it helps them in their dealings with the European Union. The EU's already fairly strict rules on privacy-which it considers a fundamental human right-are being tightened further. The time-consuming and expensive legal hoops the EU makes American internet firms jump through, to be allowed to handle Europeans' online data, will become more demanding.

If by passing its own online-privacy "bill of rights" America can convince the EU to ease this legal burden, then it will be an important win for American companies, says Joel Reidenberg, a professor at Fordham University's law school. Google, Facebook and others will no doubt be tracking-both online and offline-the progress of EU-American talks on this matter very closely.

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Greek business nightmares

Cursed are the cheesemakers

Greece's government is promising to make life less dismal for businesspeople. It has a long way to go



"GREECE has been a leftist country since 1974," laments Yannis Stournaras, head of IOBE, a private-sector think-tank. Perched behind his desk in an office not far from the Acropolis, Mr Stournaras argues that the pendulum of Greek politics swung to the left after the end of the military dictatorship and has stayed there ever since. The result is a state-heavy economy with excessive and contradictory legislation that is strangling the private sector.

Greece's rankings in the World Bank's latest annual "Doing Business" survey, published in November, were strikingly poor for a rich, supposedly modern country that has been a European Union member for 30 years. As other governments around the world pushed ahead with liberalising reforms, Greece slipped 12 places in the bank's league table of 183 participating countries (see chart), ending up behind Paraguay and Bangladesh. Opening a new business in Greece is well nigh impossible; closing one is somewhat easier.

Business in fetters

Greece, ease of doing business
Rank out of 183 countries

Indicator	2011 Rank	Change in rank on 2010
Protecting investors	154	▼1
Registering property	153	▼46
Starting a business	149	▼3
Overall	**109**	**▼12**
Getting credit	89	▼2
Enforcing contracts	88	▲1
Trading across borders	84	▼3
Paying taxes	74	=
Dealing with construction permits	51	=
Closing a business	49	▼6

Source: World Bank

Greek companies are constrained by a raft of what locals call "counter-incentives"-laws and bureaucratic hurdles that make it hard to do business. IOBE has counted 250 of them. Some of these are now being abolished thanks to the tough austerity and reform package that was the condition for a euro110 billion ($145 billion) loan from the EU and the International Monetary Fund, which prevented Greece from defaulting last year. On March 12th the EU gave Greece more

time to repay the union's euro80 billion contribution to that bail-out package, and cut the interest rate, in return for the Greek government promising to raise euro50 billion from privatisations in the next five years.

The Socialist government is making some progress in opening a closed economy against resistance from a myriad of vested interests. It forced open road haulage, one of the most notorious of nearly 70 closed-shop trades and professions, by doubling the number of lorry licences. Pharmacists had to swallow the end of their 35% profit margin on prescription drugs. The privileges of lawyers, civil engineers and architects will be next.

IOBE estimates that freeing up all the closed professions could boost Greece's GDP by up to 17%. But given the huge potential gains and the country's urgent need for a growth boost, Spiros Giamas, the boss of CDMedia, a distributor of video games, wonders why the government is reforming piecemeal instead of making a bonfire of such outmoded restrictions. There is still a chorus of complaint from Greek entrepreneurs about the government's timidity in pushing its reforms.

"Sometimes you feel stupid doing business here," says Stefanos Panteliadis, the chief executive of Epirus, a maker of feta cheese in the eponymous north-western region of Epirus. Every year Mr Panteliadis is vexed by the legal requirement for companies to publish their balance-sheets in two national newspapers and a regional one. Although publishers welcome the revenues this outdated rule brings, it is a pointless expense for companies which, like Epirus, make all their figures available on the internet. The only regional paper in Epirus charges local companies even higher advertising rates than national dailies, because they have no alternative.

This is one example of many business-unfriendly laws that are obsolete or so complex that they leave plenty of scope for bureaucrats to interpret them arbitrarily. Greece's previous government, run by the conservative New Democracy party, passed a law on promotional pricing in supermarkets that required goods to be labelled with as many as nine prices, including the cost before and after the promotion, with and without tax, per kilogram, and so on. When the Socialists got in, they made this law more complicated still, sighs Mr Panteliadis.

More taxing than ever

Orsalia Partheni, who runs a fashion retailer and manufacturer in Athens, says that corporate taxes and social-security contributions are the biggest burden on her business. Last year, she was faced with "urgent" taxes, ad hoc levies to alleviate the country's financial crisis, which made a difficult year even trickier. She recently had to close a shop in Nea Erythraia, a fashionable part of Athens. One in every two shops in Kolonaki and Glyfada (two trendy Athens neighbourhoods) has closed, says Ms Partheni. They cannot pay the high rent for the location as well as the additional one-off payments of more than euro100,000 that landlords are insisting on passing on to tenants.

Vanya Veras gave up even trying to set up a company because she found the process too expensive, too complicated and too long. She freelances as an environmental consultant in partnership with Oikosteges, a company that makes rooftop gardens. There is no shortage of pointless laws in her line of business. While writing a waste-management plan for a municipality she discovered that for some reason composting is only allowed in industrial zones, which put an end to the municipality's plans to recycle its plant matter.

By nature and inclination Greeks are entrepreneurial. Greek immigrants in America and Australia tend to do well with restaurants, corner shops and other small businesses. Yet only the very resilient and those prepared to cut corners survive the anti-business environment back home. IOBE's Mr Stournaras believes that the current crisis will be cathartic and that after five tough years Greece will recover. It remains to be seen how many entrepreneurs can hang on until then.

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Apology: Larry Summers

Last week's Schumpeter column on Michael Porter included a quotation from Larry Summers that was from an off-the-record conversation and did not include the full context. We have apologised to Mr Summers.

Hollywood and home entertainment

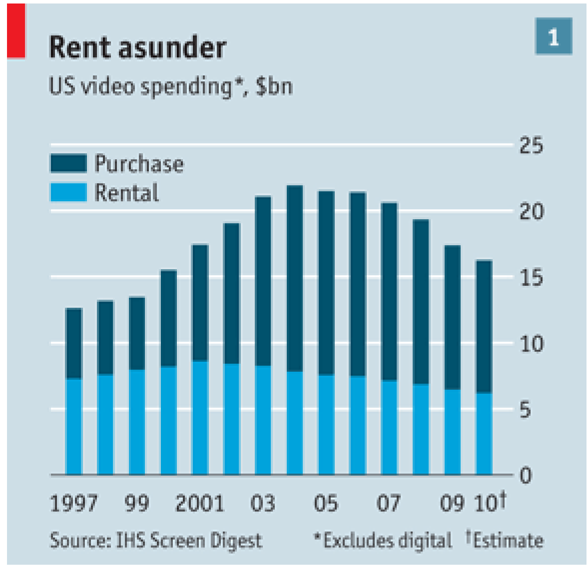
Unkind unwind

The film industry tries to revive the ailing home-entertainment business



"BE KIND REWIND", a 2008 comedy about the travails of a small New Jersey video store, is not the best film ever made about the film business. But it may be one of the most honest. Whereas most entries in this navel-gazing genre are about the making of movies-the scheming actors, the lying moguls-"Be Kind Rewind" is about the unglamorous but vital business of getting them into customers' hands. It is accurate in another way, too: it ends with the video store about to close, crushed by technological change.

Films open on big screens but make money on small ones. After a four-month exclusive run in cinemas (a "window", in Hollywood jargon) they become available as DVDs and Blu-ray discs-and, often, as on-demand videos and digital downloads. In 2010 Americans spent $18.5 billion on such things. Just $10.6 billion was spent on cinema tickets in North America. Another window opens about six months later, when films are sold to cable- and satellite-television companies. Perhaps two years after that they will be sold to free broadcast channels. Like cars, films become cheaper as they age.



Yet the once lucrative home-entertainment market is ailing. A steep decline in DVD sales has more than cancelled out growth in high-definition Blu-ray discs and electronic downloads. The overall home-entertainment market stands at 78% of its peak level, even before adjusting for inflation (see chart 1). Few think the drop is over. And nobody appears to believe that the market will recover the heights of five years ago. "In retrospect, that was a bubble," says Tom Adams of IHS Screen Digest, a leading analyst of the market.

Mid-budget films of the kind that tend to be nominated for awards were the first to be caught in the downdraft. Partly as a result, studios have pruned their output. They are concentrating on big-budget spectaculars that will draw people to cinemas around the world. In 2006 the members of the Motion Picture Association of America released 204 films, including 80 from their subsidiaries-partly independent outfits like Miramax and New Line. Last year the studios released 141 films, including just 37 from subsidiaries. Truly independent film-makers, who have lost not just home-entertainment revenues but also outside financing, are struggling even more than usual. If you think there are fewer thoughtful, well-crafted films around these days, you are right.

The DVD slump has also divided Hollywood. Film executives, though they eat in the same few restaurants and attend the same parties, cannot agree on the best way of reviving the home-entertainment market, or even on what has caused it to slump. But so perilous is their position that some bold experiments are under way. Chaotically, but quickly, the studios are about to bulldoze conventional wisdom about how films should be sold.

About one thing the studios are fairly sure. Piracy, which was widely viewed as the greatest danger facing the film business a few years ago, has been eclipsed as a threat. Illicit streaming and downloading are certainly rampant in countries like Russia and China. But such places never had much of a home-entertainment market. They have simply moved on from pirate DVDs to illegal streaming. Piracy there represents growth forgone rather than losses.

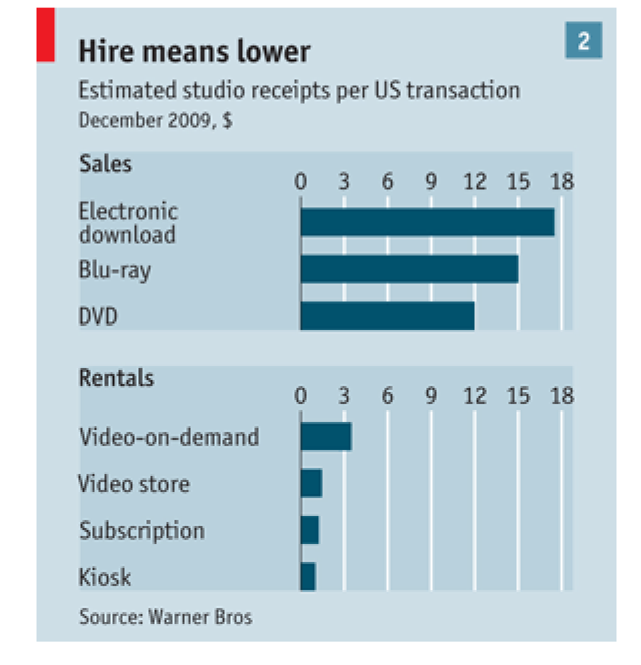
In developed countries, particularly America (by far the biggest home-entertainment market), people have switched from buying to borrowing. Since 2007 the number of films rented in America has grown by 10% even as spending on home entertainment has steadily declined. People still go shopping for animated films that will keep their children quiet, and for beloved blockbusters: more than 30m DVDs and Blu-ray discs of "Avatar" have been sold worldwide. For everything else they are turning to a range of innovative, legal and-best of all-cheap alternatives.

One of the new entrants that worries the studios can be seen in a shopping mall in Crenshaw, at the smart end of south-central Los Angeles. The Walmart that anchors Crenshaw Plaza carries a good selection of DVDs and Blu-ray discs. On a recent visit "Red" could be had for $15 plus sales tax and "Toy Story 3" for $19.96. A triple pack containing a DVD, a Blu-ray disc and a digital copy of "Despicable Me" was going for $24.96.

On their way to the DVD section, however, many of Walmart's customers pass a cheaper option. In the entrance foyer, next to a fizzy-drinks machine, sits a red kiosk that rents films by the day. "Red", "Despicable Me" and "Toy Story 3" are all available on DVD for just $1 plus tax. Blu-ray discs cost only a shade more at $1.50 a day.

Rise of the machines

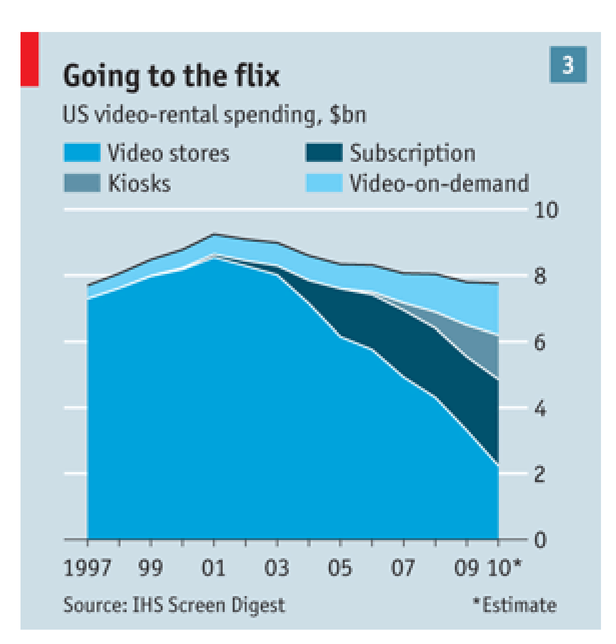
This "Redbox" is owned by Coinstar, a firm that also builds change-counting machines. It is one of almost 30,000 that have been installed since 2006, many of them in the same Walmart stores that together represent the single most important retail outlet for film discs. A few years ago Hollywood and incumbent video stores like Blockbuster were focused on the threat from piracy and video streaming. Instead they have been undercut by a device that resembles a cross between a cash machine and a 1950s jukebox.



A studio would almost always rather sell a film than rent it. But if someone is determined to rent, the studio would rather he did it somewhere other than a kiosk. Last year Warner Bros estimated the average amount it received from various transactions (chart 2). At the top of the list is an electronic download, a high-margin sale that earns $17.50 for the studio. The most profitable form of rental is a video-on-demand delivered through a cable or satellite set-top box, which is worth $3.50. Video-store rentals are worth $1.45. At the bottom of the scale are kiosk rentals. They are worth just $1 each to the studio, and would be worth even less if people were more punctual about returning their DVDs.

If Redbox worries the studios, Netflix terrifies them. That firm sends DVDs through the post to subscribers, who pay a monthly fee based on the number of films they want to keep at one time. It also allows them to stream films and TV shows at no extra charge. Viewers can watch on laptops or TVs connected to the internet, either directly or through games consoles. Netflix has more than 20m subscribers-up from just over 9m at the end of 2008. Its success has attracted rivals, including Amazon: the e-retailer bought LOVEFiLM (a similar but inferior European service) in January. But Netflix has a terrific reputation among its customers and a considerable head start. It will be hard to catch.

Sandvine, a firm that helps internet-service providers manage their networks, reckons Netflix accounts for 20% of non-mobile internet traffic in America during the evenings. Yet the humdrum business of sending discs through the post is still crucial. Thanks to a legal doctrine developed in the days when most video stores resembled the tiny business in "Be Kind Rewind", discs can be rented as soon as they go on sale to the public. Netflix must agree on terms with the studios to stream their films over the internet, and tends to get them about a year after they appear in cinemas, if then. But it can send anything through the post. The combination of old stuff available instantly and newer stuff by mail has proved immensely appealing.



The explosive growth of Netflix and Redbox has crippled video stores (see chart 3), including the once mighty Blockbuster chain. Loaded with debt, it filed for bankruptcy last year. Similar pressures are building elsewhere. Other countries have not seen such disruptive change as America, partly because their laws do not favour rental outfits so strongly. But Japan, which also has streaming and film-rental kiosks, has seen video purchases decline twice as fast as rentals. Netflix has expanded into Canada and may well spread further. Not surprisingly, the media companies are digging in against the threat.

"I have nothing against $1 rentals-at some point," explains Kevin Tsujihara, head of home entertainment at Warner Bros. He just doesn't want cheap rentals competing with disc sales. So last year Warner Bros, Fox and Universal Studios struck deals with Netflix. The service would keep its hands off their movies for 28 days, to give them a chance to sell in shops and in high-street video stores-in effect creating a new window. In return, the studios allow Netflix to stream more old films and television shows. Sony keeps big-budget films out of Netflix's hands for 28 days but not smaller films. Attempts to impose similar terms on Redbox have been more fraught: the firm took the studios to court while attempting to fill its boxes with DVDs bought from retailers.

Shattered glass

Fox and Warner Bros claim that holding films back from cheap rental services has resulted in a modest bump not just in DVD sales but also in rentals from shops like Blockbuster, which continues to rent films as soon as they are released. Others believe the effect has been small or nonexistent. "The consumer is not as sensitive to the window as we are," suggests David Bishop, head of home entertainment at Sony. Some hint the window should be longer than 28 days.

It may be that many consumers have learned to wait an extra month to see a film cheaply. Or they may simply be confused. Independent distributors, which are usually grateful for all the money and eyeballs they can get, have generally been happy to let Netflix and Redbox have their films. So has Disney. That company has a large consumer-products division, which brings in about as much as home entertainment. It is in Disney's interest to make sure that as many people as possible see "Cars 2", so that it can sell them Lightning McQueen toothbrushes.

Disney's stance irritates executives at other leading studios, who believe it is undermining the value not just of its own content but of everyone else's too. Netflix concurs that differences among studios have puzzled consumers. "If all the studios had moved towards a 28-day window, it would have influenced behaviour," says Ted Sarandos, chief content officer of Netflix. "But if you tell people that some movies are going to be accessible in some places, it's not going to change."

Having failed to erect a united front against cheap rentals, the studios are now muttering darkly about price increases. Netflix cut some deals to allow it to stream films and television shows when its business was small. The next round of negotiations will be tougher. The firm may be faced with a choice between reduced streaming rights or a cut in its hefty profit margin. But Netflix does not need to have every film and television programme. So large is its library, so superior is its software and so widespread is its distribution on devices that the loss of some content is unlikely to dent its appeal greatly.

Even if Netflix could somehow be brought down, the studios would still face a threat from television. Partly as a response to the rise of Netflix, pay-TV firms are making more films and programmes available to subscribers at no extra charge, often on mobile phones and tablet computers. Digital video recorders are becoming big enough to store hundreds of films. The latest set-top boxes from TiVo can search for films and television programmes across broadcast programme guides, video-on-demand menus and digital video recorders all at once. They can even suggest things to watch. People sometimes reach for a DVD when they cannot find anything to watch on TV. They may do so less and less.

For a few dollars more

The studios' next step will be to do something that was unthinkable just a few years ago: they will break the convention that cinemas have films to themselves for four months. As early as next month, several big studios (Disney, Fox, Sony and Warner Bros) are likely to begin renting films through pay-television boxes just two months after they appear in cinemas. The price will be steep-almost certainly more than that of two cinema tickets. The film will probably disappear from video-on-demand menus after a couple of weeks, before reappearing at a less eye-watering price at the usual time. For technical reasons few households will be able to receive them at first. But the principle will have been established.

The cinemas are furious. The National Association of Theatre Owners points out that box-office spending has held up well in the past few years-much better than home-entertainment sales, particularly when booming cinemas abroad are taken into account. Why would the studios hazard the one bit of the business that seems to be healthy?

Not all will: Brad Grey, the head of Paramount, says he has no desire to gamble on products that may cost $250m to produce and advertise. (Paramount is part of Viacom, controlled by Sumner Redstone, who also owns cinemas.) But the others will go ahead because they believe releasing films early on video-on-demand will not dent the popcorn market. "People go to the movies because they like to go to the movies," says Rob Friedman, head of Summit Entertainment. The most likely renters of premium on-demand videos, executives believe, are parents of young children, for whom a trip to the cinema costs $60 or $70 including the babysitter.

One hope is that offering newish films through set-top boxes will encourage people to rent more films that way. Video-on-demand has been slow to catch on, partly because couch potatoes dislike wading through alphabetical lists of titles. Mr Adams of IHS reckons the average American household spent just $17 on video-on-demand in 2010. But there is some cause for optimism. Independent distributors such as IFC Films and Magnolia Pictures are miles ahead of the big studios; they often release low-budget movies to homes even before they appear in cinemas. As a result, video-on-demand is now an important sales channel for independent film.

The second thing the studios will do this year is to try to ginger up electronic sales. Film downloads through Apple's iTunes and other digital stores have not been popular so far. They are expensive, often costing more than DVDs. They are also inflexible, points out Mitch Singer of Sony Pictures, who also leads an industry consortium known as DECE. You can take a DVD to a friend's house, pop it into a portable player or a laptop and even play it in your sport-utility vehicle. None of which is possible at present with a digital download. "People don't want to buy something that won't work on a device they might want to buy in two years' time," says Mr Singer.

All the big studios apart from Disney (once again going its own way) will start offering electronic copies of films that conform to a single format later this year. Buy a film, either as a download or as a Blu-ray disc that comes with digital rights, and a token will be stored in your account. In theory, you should then be able to play the film on television through your existing set-top box, download it to your laptop and your smartphone, and perhaps burn an extra copy to a DVD. Buying a film should begin to seem more appealing than renting it or downloading it illegally.

This method has another potential advantage for the studios: it should allow them to market their films more precisely. At present, whenever a studio launches a film it must create a marketing plan almost from scratch. Not only do the studios know much less about individual tastes than firms such as Netflix or Amazon. They are likely to know less than a shampoo-maker. But when people download films they leave clues about their tastes-clues that could be assembled into databases and used to target people who might be interested in the next release.



Steady hand required

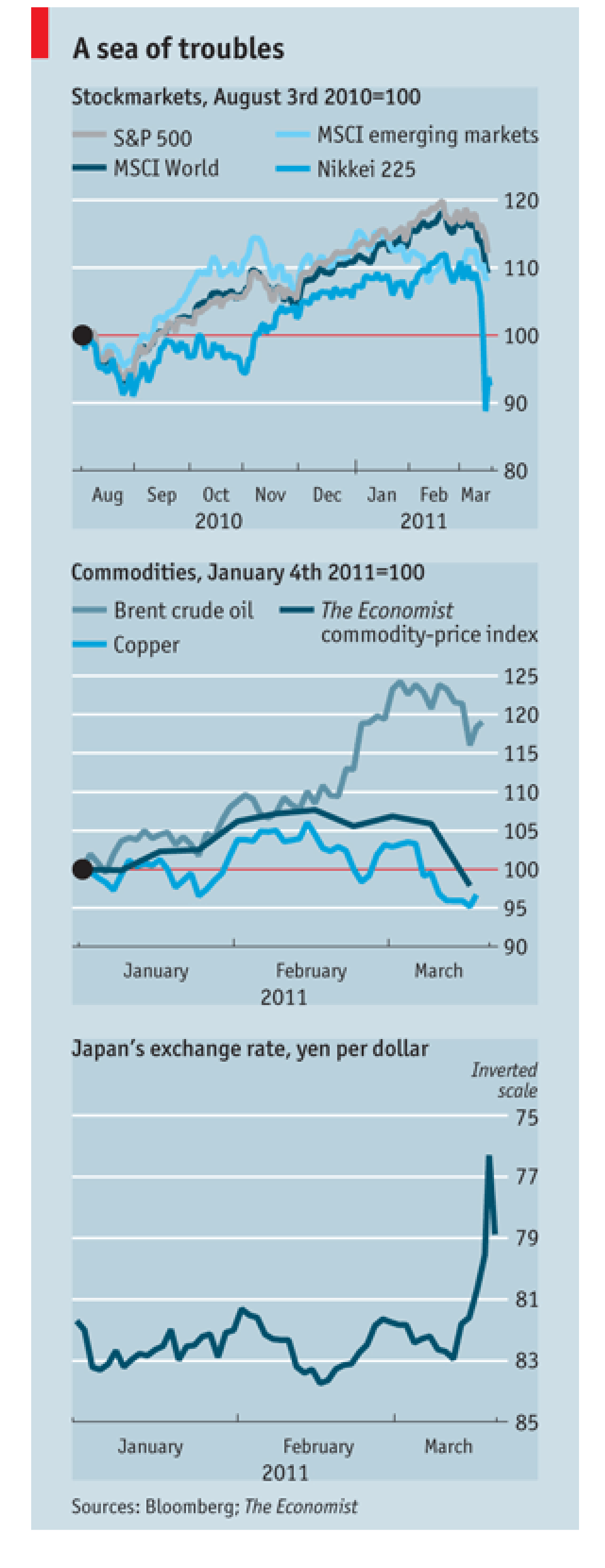
Some studios are beginning to think along these lines. On March 8th Warner Bros announced that it would start renting films through Facebook. It will hope that fans will do some of the marketing for it on the social network. But there is an uncomfortable caveat. In order for digital distribution to take off, the studios will probably have to bring prices down from their current heights. Internet shoppers have learned to expect bargains. If they don't get them, many will find illegal ways of getting hold of films without paying. Some Hollywood executives hope that digital downloading can shore up profit margins eroded by the collapse of DVD sales. That may well prove forlorn.

It will not be easy for an old industry to develop an entirely new set of muscles. But Hollywood must become more consumer-oriented. The alternative is watching the most lucrative part of its business slacken, slur and fail, like an old, worn-out VHS tape.

Financial markets

Aftershocks

The Japanese earthquake is the latest piece of bad news to unsettle investors



WHEN disaster strikes, the reaction of many investors is to scoot first and ask questions later. The Japanese earthquake and tsunami, and the subsequent nuclear crisis, prompted some very sharp falls in equity markets this week.

The Nikkei 225 average in Japan fell by 6.2% and 10.6% on the first two days of the trading week respectively, before recovering a little (see top chart). Losses were more subdued in international markets but global equities still suffered their biggest one-day loss for seven months on March 15th. In America the Dow Jones Industrial Average slipped well below the 12,000 mark, which it had regained in early February for the first time since the collapse of Lehman Brothers.

The gloom was not all down to Japan. Since February markets have been caught off-guard by a combination of geopolitical risk, rising commodity prices and the prospect of tighter monetary policy. Political unrest in north Africa and the Middle East had already pushed oil prices up by almost a quarter, with Brent crude rising from $93.33 a barrel on January 7th to $116.35 on March 2nd. That brought back unwelcome memories of 2008, when an oil price of $146 a barrel contributed to the recession. With other commodity prices also driving up headline inflation, the European Central

Bank signalled that it was on the brink of raising interest rates. The Bank of England, which has allowed British inflation to drift well above its target, was under pressure to follow suit.

Rate rises would prove a particular challenge for those euro-area countries that are still struggling with their sovereign-debt burdens (see article). Much of the European Union is already attempting to tighten fiscal policy. That is a worry for investors who recognise that the global recovery has owed much to the effects of fiscal and monetary stimulus. The level of official support for the markets has been gradually declining: China has been pushing up interest rates and raising reserve requirements in the banking system in an effort to restrain growth.

So the terrible news from Japan came at a time when investors were already looking to reduce their risk exposure. The earthquake adds two further threats to the global economy (aside from the risk of a genuine nuclear catastrophe). The first is that global supply chains will be disrupted, particularly in the electronics industry. Texas Instruments said that two of its Japanese chip-making plants had been damaged; one of them, in Milo, was responsible for about 10% of the company's output. Freescale Semiconductor said it had stopped production at its plant in Sendai, close to the centre of the quake. Production was also affected at a wide range of subcomponent plants.

A report by Daiwa Securities said that the closure of plants operated by Hitachi Chemical, Sanyo Electric and Sony would affect the supply of lithium-iron batteries. Production of printed circuit boards may also be disrupted since Japan is responsible for supplying 90% of one of the epoxy resins used in their manufacture.

Companies that depend on Japanese suppliers will try to find alternative sources in Asia. But that will take a while, and modern businesses run "just-in-time" inventory policies with very little slack. Industrial production may be adversely affected in the interim.

A second, longer-term threat stems from attempts to rebuild Japan's economy. Although such reconstruction will boost Japanese GDP, it comes at a cost. Some of this burden will be borne by global insurers (see article), but some of it will be financed by Japanese investors repatriating assets, as happened after the Kobe earthquake of 1995, with potentially negative effects in other markets.

Capital is already on the move. Investors reacted to news of the disaster by cutting their more speculative positions, regardless of whether there was a direct link to events in Japan. The currency that took the biggest hit, for example, was the Australian dollar, which has been trading as a commodity-linked asset. It fell in line with many raw-materials prices, as traders took profits after a run-up earlier in the year.

Even oil took a temporary hit (see middle chart) despite the continuing conflict in Libya and despite the likelihood that fears over the safety of nuclear energy will make economies more dependent on fossil fuels. The oil price rose again on March 16th as continuing unrest in Bahrain, amid the presence of foreign troops, sparked fears of wider conflict in the Gulf region.

The yen came under severe upward pressure, surging on March 16th to its highest level since the second world war (see bottom chart), before falling back. The Bank of Japan tried to counteract that process, easing monetary policy in a bid both to support the markets and to prevent rapid yen strengthening from damaging the prospects of exporters.

Government bonds in America and Germany benefited from the flight to safety that usually follows bad news. Japanese bonds were rather stable but the cost of insuring Japanese government debt against default rose sharply, as investors contemplated the long-term costs facing a government that already has gross debt of more than 200% of GDP.

In equities, the widespread sell-off may have been a reaction to the overoptimism that prevailed earlier this year. A survey of global fund managers in February, conducted on behalf of Bank of America Merrill Lynch, found that a net 67% were overweight equities (relative to their normal portfolio allocation). The same poll found that a net 51% expected the global economy to strengthen over the following 12 months. Polled again in March, investors had become much less sanguine.

Just as fund managers were too upbeat last month, some argue that the current pessimism is overdone. After all, the sharp fall in commodity prices over the past week, if sustained, will be good news for developed economies. Both the European Central Bank and the Bank of England may now be cautious about raising rates until the full impact of the earthquake becomes clear. Futures markets are pricing in lower rates than they were before the disaster.

Bull in your court

According to Paul Niven at F&C, a fund-management group, "the extent of the declines in asset prices reflects panic selling with signs of investors exiting at any price. Provided that the global economy can maintain momentum-which we expect-then risk assets should recover poise and make gains from current levels. Relative value in Japan has never been as pronounced as it is today."

And some bullish arguments remain intact. The corporate sector is performing well. Morgan Stanley says that the profits of S&P 500 firms are expected to rise by 15.4% this year, after growing by 39.3% in 2010. European profits are expected to grow by almost 15% this year, according to Goldman Sachs.

Nevertheless, the markets (and central banks) still face a tricky high-wire act for the rest of the year. On one side, there is the danger of rising inflation, a prospect highlighted by American producer-prices numbers for February, which showed a 5.6% annual rise. On the other, there is the risk of falling back into recession. It could be a wobbly summer.

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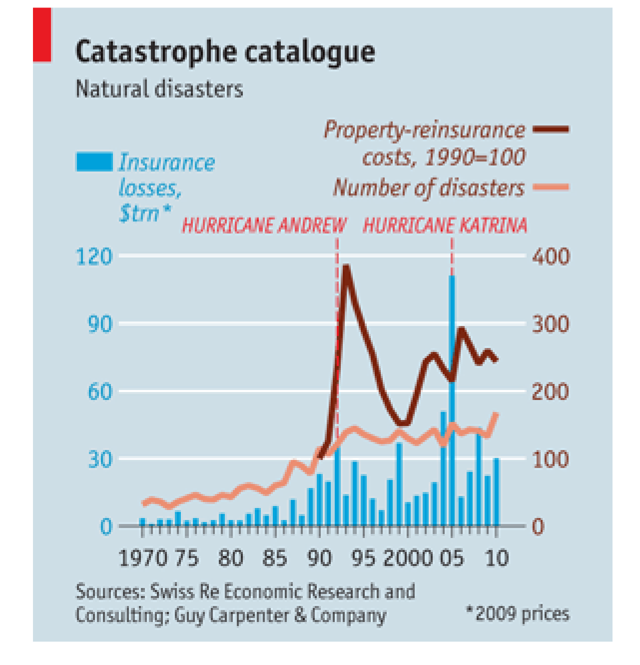
Reinsurance after Japan's quake

When nature attacks

Bearers of catastrophe risk are likely to ride this one out



REINSURANCE companies and bad news have a twisted relationship. Catastrophes give insurers a reason to protect themselves by taking out reinsurance, but they can also burn through capital. Disasters can hurt profits in one year, but also lead to a rise in premiums in following years-witness the effects of Hurricane Andrew in 1992 and Hurricane Katrina in 2005 on catastrophe-reinsurance rates subsequently (see chart). The disaster in Japan, for all the terrible suffering it has caused, looks set to have a more muted effect.



Global insurers, apart from those in Japan itself, were not heavily exposed to catastrophe risk in the country. Nuclear risks tend not to be privately insured. The semi-public Japan Earthquake Reinsurance Company will bear the brunt of the losses-estimates of how high they will go are still very provisional-and the government any further excess, although payouts may come to only half of the total damage.

So the share-price falls experienced by major reinsurers such as Swiss Re and Munich Re, of around 10% over the three working days after the quake, were probably overdone. Non-Japanese reinsurers are likely to suffer combined losses of $10 billion-20 billion, according to James Shuck, an analyst at Jefferies International. That may dent their expected profits for 2011 but will not eat into capital.

The reinsurance sell-off is not totally irrational. Share indices have generally fallen since the quake, and insurers rely on equity-market investments to bolster capital and performance. And the Japanese disaster comes at a lean time for reinsurers. Last year was catastrophe-strewn, thanks to earthquakes in Haiti, Chile and New Zealand, as well as an explosion at the Deepwater Horizon oil rig. Even so premiums barely rose, perhaps because there was too much spare capacity in the reinsurance industry. Floods in Australia and another earthquake in New Zealand had already sapped chances of handsome profits this year when the tsunami struck.

If this disaster does not lead to losses high enough to raise premiums, might the perception that extreme events seem to be on the increase? If the industry reached a consensus that the risk of natural catastrophes had grown, that would indeed push rates up. As a rule of thumb, reinsurers have tended to reckon that claims for catastrophic events (those expected once in every 200-250 years) will equal about 6.5% of the annual premiums they take. In recent times that assumption has been too low. Munich Re, for example, experienced catastrophe losses of 11% of net premiums in 2010. Hannover Re experienced catastrophe losses in 2010 that were 21% higher than the amount it took in on premiums.

That probably reflects one disaster-prone year and the fact that more things are being insured, rather than rising risks of calamity. Sentiment drives insurance premiums as much as mathematical models and past experience, however. The catastrophe in Japan may yet lead to higher premiums for that reason, if no other.

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The euro-debt crisis

Muddle, fuddle, toil and trouble

European leaders boldly decide to carry on muddling through



A BARGAIN, but not a grand one. Euro-zone leaders surprised many on March 12th by agreeing on the main elements of a deal to salve Europe's sovereign-debt crisis. With negotiations becoming fractious and markets unnerved by further ratings downgrades on Greek and Spanish debt, there had been fears that a deal might not be reached by a deadline of March 25th, when Europe's heads of governments conclude their next meeting in Brussels. In the event, a special summit of euro-area leaders hammered the essentials out two weeks ahead of schedule.

A deal may have arrived early, but it was lightweight, too. That largely reflected the wishes of Angela Merkel, the German chancellor, who is hemmed in by antipathy among taxpayers back home to propping up profligate Greeks and others. The effective lending capacity of the European rescue funds will be bumped up to meet its original goal of euro500 billion ($695 billion) through higher guarantees and injections of capital, though the precise mix and timing have yet to be spelt out. But the main fund, the European Financial Stability Facility (EFSF), will not be allowed to intervene in secondary government-debt markets, a job being undertaken reluctantly by the European Central Bank.

The EFSF will be able to purchase the bonds of rescued governments when they are newly issued. But that is likely to be of use only when those countries want to tap markets again. Meanwhile, high sovereign-debt yields in secondary markets have a knock-on effect on the borrowing costs of firms and banks in affected countries.

The deal held out the prospect of lower borrowing costs on rescue finance, subject to tougher conditions. The Greek government has secured a reduction of one percentage point in the interest rate charged on euro80 billion of bilateral loans from euro-area countries arranged before the EFSF was set up. The maturity of these loans, and of an additional euro30 billion from the IMF, will be extended from three to 7.5 years. In return the Greeks say they will privatise public assets worth euro50 billion-though they will not sell off islands, despite calls from *Bild*, a German tabloid.

The new Irish government, led by Enda Kenny (pictured, with France's Nicolas Sarkozy), had also hoped to extract a lower interest rate but came away empty-handed. The price for such a concession was that Ireland raise its low corporation-tax rate. Other euro-area countries, notably France, have long been unhappy about this tax competition. But the Irish refused to give ground on their 12.5% rate, which they regard as crucial for retaining the country's appeal to foreign investors.

The deal also included a fleshed-out version of the "competitiveness pact" unveiled in February largely at the behest of Germany. The idea is to prevent a recurrence of the debt crisis by whipping euro-zone laggards into Teutonic shape through economic and fiscal workouts. Now redubbed the "pact for the euro", it stipulates that all euro-zone countries put into law a pledge to get a grip on public debt.



Traders responded favourably to the deal: spreads tightened on the bond yields of peripheral euro-zone countries, compared with German Bunds. But prior attempts to resolve the crisis have brought only temporary relief (see chart) and this agreement is likely to be no different.

An early shock could be supplied by Portugal, whose credit rating was downgraded this week. Despite the Portuguese government's decision on the eve of the summit to intensify its fiscal retrenchment, the country still looks likely to require a rescue. On March 16th Portugal had to raise yields on a sale of 12-month government bills by 27 basis points compared with the previous auction a fortnight earlier.

If Portugal did ask for help, it could prove another nasty moment for the euro area. The rescue funds are big enough to cope with Portugal but the fear is still that confidence in neighbouring Spain, a much bigger economy, would be shaken. Even if that peril is avoided, the paths to rehabilitation for Greece and Ireland look so difficult-the black hole that is the Irish banking system could get still deeper, for instance-that it is hard to see how they can escape without an eventual debt restructuring. After promising much, European leaders have delivered too little.

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Data-driven finance

Go figure

A new class of internet start-ups is trying to turn data into money

ASKING a friend for a loan is a quick way to tide you over till the end of the month. But Wonga, a British internet firm, is almost as fast. Those in need of cash give the service some basic information about themselves. If Wonga considers them trustworthy, the money—as much as pound400 ($641) for up to 30 days for first-time users—arrives in their accounts within 15 minutes.

Consumer advocates are highly critical of the service: its annual interest rate currently exceeds 4,000%. But Wonga, which uses funding from its venture-capital backers to make loans, is attracting attention for other reasons. The firm is one of a growing number of internet start-ups that mine unconventional forms of data to offer financial services.

Klarna, a Swedish company that counts Sequoia Capital, a noted venture-capital firm, among its financial backers, allows consumers to shop online by simply typing in their date of birth, name and address. Klarna fronts up the payments and charges retailers a fee for making online purchases easier. Shoppers pay only once they have received the goods. ReadyForZero, a start-up in Silicon Valley, lets people see all their credit-card debts in one place and puts together a plan to pay them off.

Of course, conventional lenders sift through information about borrowers to decide whether someone is a good risk. But the start-ups are different. First, they combine data from many sources. Klarna started by looking at conventional credit scores, but it says that the actual behaviour of shoppers has much more "predictive power", in the words of Sebastian Siemiatkowski, Klarna's chief executive. The company receives a lot of data from online stores, including things like the time of purchase and whether the consumer's name and address were typed or copied in (the latter is more likely to signal fraud). Wonga draws on "all publicly available data", in the words of Errol Damelin, Wonga's boss, who does not want to be more specific for security reasons. ReadyForZero accesses data on users' credit-card transactions.

Second, decisions are made very quickly. Klarna and Wonga feed all the data through elaborate algorithms which determine, almost in real time, how likely it is that a user with a certain data profile will default. Consumers who shop online at 3am may find themselves among the 20% of buyers who get rejected by Klarna. Having a mobile phone with a contract helps to get money from Wonga (which says "no" to 70% of applications). But no single factor is decisive, says Mr Damelin. "It's about how the data connect to each other." Klarna's algorithms are regularly updated to reflect new types of behaviour.

Third, whereas other lenders may play up their branch networks or customer service, data are the start-ups' big source of advantage. ReadyForZero's service is free: users essentially pay with their data. It is still trying to figure out how it can use this information to make money, says Rod Ebrahimi, one of the firm's founders. One idea is offering credit scores that are more fine-grained than those currently provided.

All three start-ups are already pretty popular. Wonga claims to make more than 100,000 loans a month. About 5m consumers in six European countries have used Klarna to pay for their online shopping. Users of ReadyForZero have registered nearly $30m in credit-card debt only six weeks after the service went live.

Yet the firms' success is hardly guaranteed. One risk is financial regulation. Wonga just had to increase the interest rate it shows on its site by 1,500 percentage points because an EU rule required it to calculate interest differently. Online privacy is another issue: ReadyForZero's users may balk if they find that their data, albeit anonymised, will be used elsewhere.

Even if these start-ups fail, the trend they represent is unstoppable, says Mr Damelin. As such offerings grow, "it will become less and less obvious why you would need a retail bank." That is wishful thinking. But for financial firms that do not use data smartly, the number's up.

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Buttonwood

The old Bill

Stopping quantitative easing may be harder than starting it



BILL GROSS is the most famous and experienced bond-fund manager in the world. So when he says PIMCO's Total Return, the $237 billion fund which he manages, is avoiding Treasury bonds, investors should take notice.

Mr Gross is particularly worried about the effect of quantitative easing (QE) by the Federal Reserve, the second round of which is due to expire in June. He has described this process, whereby the Fed creates money to buy both mortgage-backed securities and Treasury bonds, as a form of pyramid or Ponzi scheme.

PIMCO reckons the Fed has been responsible for 70% of recent Treasury purchases, with foreigners buying the other 30%. "Who will buy Treasuries when the Fed doesn't?" asks Mr Gross, adding that the danger is of a spike in bond yields as private investors demand a higher return to compensate them for the risks of inflation or dollar depreciation.

He cites a number of reasons why yields may be at least 150 basis points (one-and-a-half percentage points) too low. First there is normally a rough relationship between yields, currently 3.3% for ten-year Treasury bonds, and nominal GDP growth projected at around 5% a year. Second, real five-year Treasury-bond yields have averaged about 1.5% in the past; they are currently slightly negative. Third, the short-term Fed funds rate is around 475 basis points below nominal GDP growth, compared with an historic average of 75 basis points.

To some, this may seem naive. The end of QE2 has been well signalled. Markets have had time to adjust. Mr Gross's own actions indicate that this is the case: he has sold his Treasury-bond holdings in advance. Indeed, markets don't seem worried at the moment; Treasury-bond yields have fallen over the past month.

Nevertheless, it is legitimate to worry whether getting out of a QE programme will be as easy as getting into it. (This problem also faces the Bank of England and the European Central Bank.) It is not simply a matter of ceasing to buy bonds. Unless they want to end up with a permanently bigger balance-sheet, central banks must offload those bonds they have already bought.

It is no answer to say that the programme will wind itself up naturally as the bonds mature. Unless the government concerned is running a surplus by that stage (dream on), maturing bonds need to be refinanced. So the private sector will have to absorb not only that year's financing programme but the surplus offloaded by the central bank. This is no small matter. The Fed has an asset pile of some $2.6 trillion, of which just under half is Treasuries.

Herein lies the rub. In what circumstances would investors be most keen to buy more government bonds? When the economy is struggling. But central banks will be highly unlikely to reverse QE at that stage. In any case, cynics suspect the problem with QE is that there may never be a moment when central banks feel confident enough to unwind it. After all, American GDP grew by a respectable 2.8% last year and growth of more than 3% is forecast for this year. Yet this week's Fed policy meeting indicated that the second round of QE would still be completed.

As the programme has evolved so have the justifications for QE. In testimony to Congress on March 1st, Ben Bernanke, the Fed's chairman, cited the evidence of its success: "Equity prices have risen significantly, volatility in the equity market

has fallen, corporate-bond spreads have narrowed, and inflation compensation as measured in the market for inflation-indexed securities has risen to historically more normal levels. Yields on five- to ten-year nominal Treasury securities initially declined markedly as markets priced in prospective Fed purchases; these yields subsequently rose, however, as investors became more optimistic about economic growth and as traders scaled back their expectations of future securities purchases."

Note that Mr Bernanke seems to treat both lower and higher bond yields as evidence for the success of the policy. And note also how his first two references are to the recovery in the stockmarket. His big speech on QE, back in January 2009, did not mention share prices at all.

If it is vital to maintain stockmarket confidence, then equity jitters-whether caused by Japanese earthquakes, European fiscal problems or something else-are a reason to keep QE going. And the bigger the programme, the harder it is to unwind. Mr Gross is right to worry.

Economist.com/blogs/buttonwood

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China's economy

Decelerating

China's government may at last be getting a grip on its banks

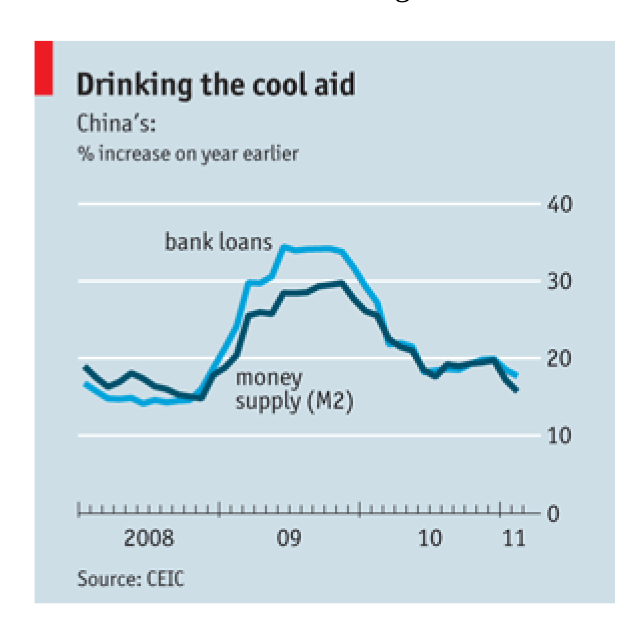


THE arrival of rain and snow on China's parched northern plain has raised hopes that the country's crop of winter wheat will fare better than feared. Food prices, which rose by about 11% in the year to February, have made a big contribution to China's consumer-price inflation, now running at 4.9%. But if drought is responsible for some of China's price pressure, a deluge of credit is to blame for the rest. So China-watchers were quick to welcome a turn in the monetary weather this week.

The country's broad money supply (M2), which includes currency and a variety of bank deposits, grew by 15.7% in the year to February, slower than expected. Monetary aggregates are an important target for the People's Bank of China (PBOC), the country's central bank, much as they were for Western central banks in the heyday of monetarism. Unfortunately, these targets can be just as elusive in China as they proved to be elsewhere: M2 has exceeded the

government's intended limit in nine of the past ten years. But February's figure will give the PBOC fresh hope of remaining within its 16% target for this year.

As well as targeting the money supply, China's authorities also strive to set limits on credit. China's banks added 535.6 billion yuan ($81.5 billion) of new loans last month, again a lower figure than expected. Their February lending was consistent with an annual total of 7.88 trillion yuan, according to calculations by Wensheng Peng of China International Capital Corporation. This is not too far above the 7.5 trillion yuan that Liu Mingkang, chairman of the China Banking Regulatory Commission, reportedly believes is consistent with the government's monetary targets.



Not everyone puts much faith in these credit figures, however. Fitch, a ratings agency, has described how banks have moved lending off their books using a variety of dodges, such as packaging loans into securitised products with the help of lightly regulated trust companies. It estimates that China's banks lent over 11 trillion yuan in 2009, far in excess of both the official figure of 7.9 trillion yuan and the official quota of 7.5 trillion yuan. Weaning China off these credit injections is not easy. The economy cannot get by with trillions less overnight without "seriously stunting growth," Fitch wrote in December. "Hidden channels are likely to continue to fill this gap so long as demand remains high, supply tight, and oversight lenient."

An alternative way to measure the availability of credit is simply to ask people. Market News International, a news agency owned by Deutsche Borse Group, regularly surveys 186 listed Chinese companies about the business conditions they face. In the main, business is still brisk, its February survey revealed. But companies also said that credit was as tight as it was in June 2008, when the authorities were battling against 7-8% inflation. This gap between business activity and constrained credit will close in due course, argues Peter Redward of Barclays Capital. And given that Wen Jiabao, the prime minister, has made fighting inflation a priority, it is likely that business will fall into line with credit, not the other way around.

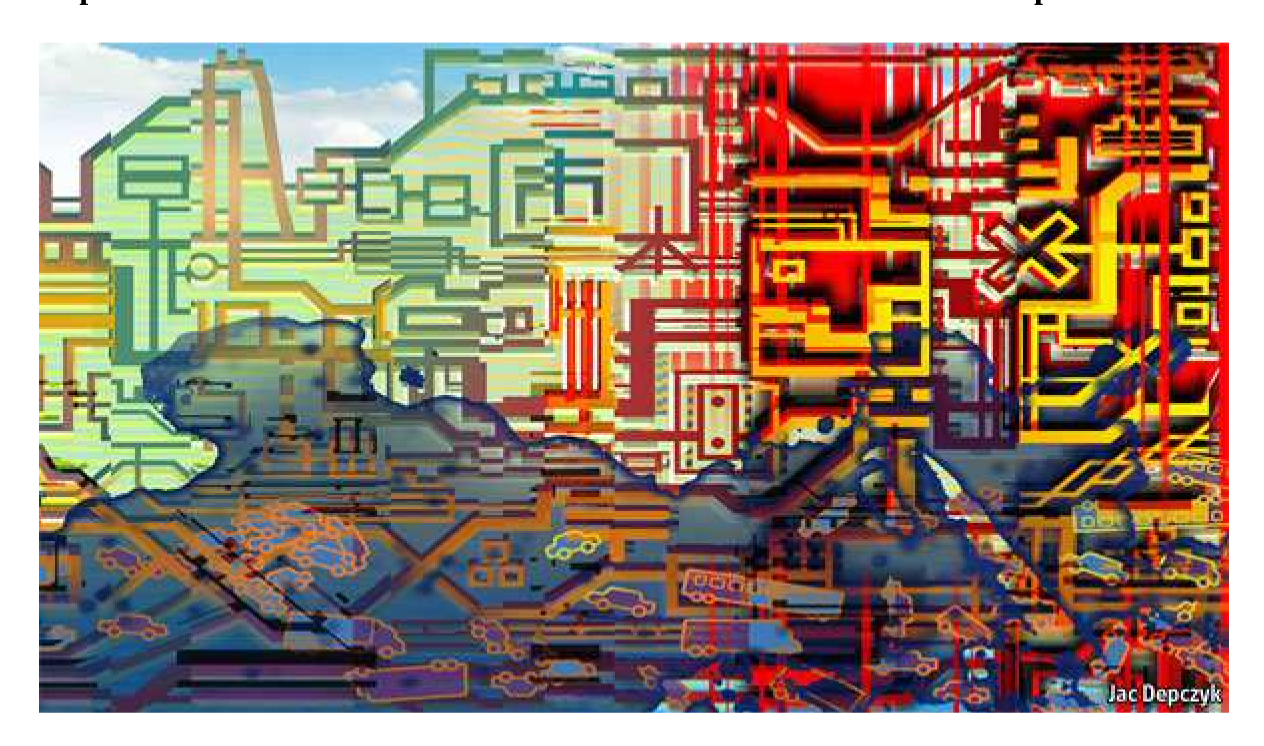
Perhaps the first signs of that appeared in China's retail sales. They were 15.8% higher in January and February than in the same two months of 2010-having grown by over 19% in the year to December. The slowing was most pronounced in car sales, partly because the government restored a 10% sales tax on small cars that had been cut in 2009. The government was restoring it now, said Liu Shangxi, an official with the Ministry of Commerce, because "the country has ridden out the crisis". It did so largely on the back of bank lending. In recent months, that lending was threatening to carry the economy away. This week's figures were encouraging evidence that the reins are tightening.

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Economics focus

The cost of calamity

The economic impact of natural disasters is often short-lived. Will this be the case in Japan?



THE full extent of the damage from the tsunami that hit Japan's north-eastern coast on March 11th is not yet known, but early estimates of the cost are big. Rebuilding homes, factories, roads and bridges could cost as much as $200 billion, some reckon. Quite apart from these direct costs, is the disaster likely to do lasting harm to Japan's economy?

Much will depend on the success of efforts to prevent a nuclear catastrophe. Assuming the situation at the Fukushima Dai-ichi plant stabilises, the contours of the economic impact of the tsunami itself can already be discerned. Natural disasters disrupt production, much as less destructive episodes of bad weather do. In Japan the interruption to electricity supply means that output has been affected even in areas the tsunami did not directly inundate. Toyota, for example, halted production because of problems with parts and supplies. Operations were suspended in six of Sony's factories, only one of which was flooded.

But such disruption is unlikely to persist. On March 16th Toyota announced that it was restarting the production of spare parts. As with bad weather, disasters cause some output to be postponed rather than lost. When production resumes, it is likely to be at a faster clip than usual. Studies of the economic effects of past natural disasters, as well as Japan's own experience after the 1995 earthquake in Kobe, provide further reassurance. They suggest that the macroeconomic effects of the tsunami, though hardly negligible, will not be devastating and will not last very long.

How much a natural disaster reduces output over the medium term depends on a number of factors. Location matters: disasters that strike an industrial belt will be more economically crippling than ones that hit an area where little is produced; the economic effects of the tsunami would have been much worse if it had struck Japan's industrial heartland. And different kinds of natural disasters have different consequences for growth. In the medium term, not all effects are negative. A 2009 World Bank study found that by increasing soil fertility, a typical flood increases agricultural output in the year after it strikes (though output falls in the year it occurs). The benefits from higher agricultural production spill over to other sectors, and in developing countries where the farm sector is a bigger part of the economy this may be enough to lead to faster growth in manufacturing and services in subsequent years.

Earthquakes, on the other hand, have small but consistently negative effects on economic growth. This is because earthquakes do not just shut production down for a while. They also destroy factories, roads, electricity lines and offices. This destruction does not directly reduce a country's GDP, which measures the value of the flow of goods and services that an economy produces. But it does affect an economy's underlying productive capacity. The Japanese tsunami fits this template.

As long as these assets remain out of commission, the output they would have produced is, in theory, lost. In practice, this negative effect can partly be made up by using plant and machinery in areas unaffected by the disaster. Most factories do not run at full steam all the time; output from plants that are still working can be increased to make up for lost production elsewhere.

An analysis of the effect of the Kobe earthquake by George Horwich of Purdue University provides some reason to hope that this might happen in Japan. The quake ravaged many of the facilities of what was then the world's sixth-largest container port and the source of nearly 40% of Kobe's industrial output. Over 100,000 buildings were completely destroyed, and many more badly damaged; 300,000 people were rendered homeless; over 6,000 died. Yet despite this devastation in a big production centre, the local economy recovered very fast. Even though less than half the port facilities had been rebuilt by that stage, within a year import volumes through the port had recovered fully and export volumes were nearly back to where they would have been without the disaster. Less than 15 months after the earthquake, in March 1996, manufacturing activity in greater Kobe was at 98% of its projected pre-quake level.

Mr Horwich reckons that the likely reason for this rebound in output and economic activity, even as swathes of infrastructure still lay in ruins, is that output can be produced using different combinations of labour and capital. Although a disaster may destroy physical capital, things can be made using more labour or using it more intensively than before. In addition, rebuilding is easier than building up capital the first time around, because it mainly aims to replicate a pattern of investment rather than figure out what to invest in. And productivity growth may accelerate when new, and often superior, machinery is installed.

A glimmer, at least

Reconstruction itself, of course, also helps to offset the negative impact of a drop in output in the aftermath of a disaster. Business booms for builders and producers of capital goods. Disasters probably do not actually stimulate the economy because additional production in some sectors may be displacing spending elsewhere, though this is less of a worry in an economy with a lot of spare capacity. Certainly, the year of the Kobe quake was not a bad one for the Japanese economy, which grew by 1.9% in 1995 compared with 0.9% growth in 1994.

There are grounds to hope, then, that this month's terrible events will not cause lasting damage to Japan's economy. But there are worries, too. The nuclear crisis adds greatly to uncertainty. Consumer and business confidence is fragile. With interest rates already at zero, policymakers have little wiggle room. Japan's manufacturing sector is running closer to full capacity now than in the mid-1990s, making it harder to make up for lost output. When disasters occur can matter as much to the economy as how bad they are.

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Marjorie Deane internship

Applications are invited for *The Economist*'s 2011 Marjorie Deane internships. Financed by the Marjorie Deane Financial Journalism Foundation, the awards are designed to provide work experience for a promising journalist or would-be journalist, who will spend three months at *The Economist* writing about economics and finance. Applicants are asked to write a letter introducing themselves, and an original article of no more than 500 words that they think would be suitable for publication in this section. Applications should be sent to deaneintern@economist.com by April 15th 2011.

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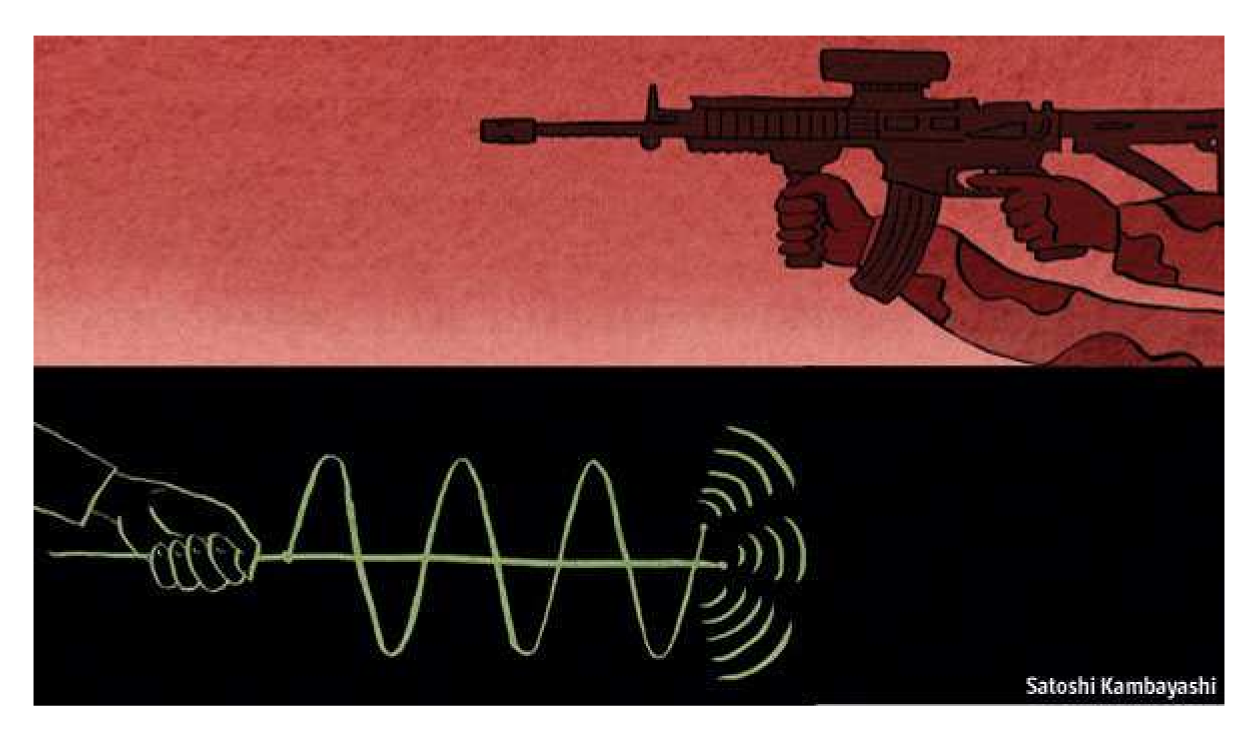
Correction: House-price table

Correction: Our latest house-price table ("Hong Kong phew-whee", March 5th) showed that Canada's housing market was 11.4% overvalued. It should have read 21%. Our apologies.

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Signalling dissent

Savvy techies are finding ways to circumvent politically motivated shutdowns of the internet



WITH a tin can, some copper wire and a few dollars' worth of nuts, bolts and other hardware, a do-it-yourselfer can build a makeshift directional antenna. A mobile phone, souped-up with such an antenna, can talk to a network tower that is dozens of kilometres beyond its normal range (about 5km, or 3 miles). As Gregory Rehm, the author of an online assembly guide for such things, puts it, homemade antennae are "as cool as the other side of the pillow on a hot night". Of late, however, such antennae have proved much more than simply cool.

According to Jeff Moss, a communications adviser to America's Department of Homeland Security, their existence has recently been valuable to the operation of several groups of revolutionaries in Egypt, Libya and elsewhere. To get round government shutdowns of internet and mobile-phone networks, resourceful dissidents have used such makeshift antennae to link their computers and handsets to more orthodox transmission equipment in neighbouring countries.

Technologies that transmit data under the noses of repressive authorities in this way are spreading like wildfire among pro-democracy groups, says Mr Moss. For example, after Egypt switched off its internet in January some activists brought laptops to places like Tahrir Square in Cairo to collect, via short-range wireless links, demonstrators' video recordings and other electronic messages. These activists then broadcast the material to the outside world using range-extending antennae.

According to Bobby Soriano, an instructor at the Philippine branch of Tactical Tech, a British organisation that teaches communication techniques to dissidents in five countries, such antennae can even foil government eavesdropping and jamming efforts. Directional antennae, unlike the omnidirectional sort, transmit on a narrow beam. This makes it hard for eavesdroppers to notice a signal is there.

Citizens banned?

Another way of confounding the authorities is to build portable FM radio stations. One broadcasting expert, who prefers not to be named but is currently based in Europe, is helping to develop a dozen such "backpack" radio stations for anti-government protesters in his native land in the Arabian peninsula. Though these stations have a range of only a few kilometres, that is enough for the leaders of a protest to use them to co-ordinate their followers. The stations' operators act as clearing houses for text messages, reading important ones over the air for everyone to hear.

Conventional radio of this sort cannot, unfortunately, transmit video or web pages. But a group called Access, based in New York, is trying to overcome that. To help democracy movements in the Middle East and North Africa get online, it is

equipping a network of ham-radio operators with special modems that convert digital computer data into analogue radio signals that their equipment can cope with. These signals are then broadcast from operator to operator until they reach a network member in an area where the internet functions. This operator reconverts the signal into computer-readable data and then e-mails or posts the information online.

Satellites provide yet another way of getting online, though they are expensive to connect to. It is, however, beyond the authorities in most places to shut down a satellite operated by a foreign company or country. The best they can do is try to locate live satellite links using radiation-detection kit similar to that supposedly employed in Britain to seek out unlicensed televisions. The result is a game of cat and mouse between the authorities and satellite-using dissidents. Tactical Tech, for example, has trained dissidents in five countries to rig satellite dishes to computers in order to get online. It advises some users to log on only for short sessions, and to do so from a moving vehicle.

Such dishes can also be repurposed for long-range internet connections that do not involve satellites. Yahel Ben-David, an electrical engineer at the University of California, Berkeley, who has designed secret cross-border links to the internet for people in several countries, does so by adding standard USB dongles designed for home Wi-Fi networks. Thus equipped, two properly aligned dishes as much as 100km apart can transmit enough data to carry high quality video. Moreover, the beam is so tightly focused that equipment a mere dozen metres away from its line would struggle to detect it.

Creative ideas for circumventing cyber-attacks even extend to the redesign of apparently innocent domestic equipment. Kenneth Geers, an American naval-intelligence analyst at a NATO cyberwar unit in Tallinn, Estonia, describes a curious microwave oven. Though still able to cook food, its microwaves (essentially, short radiowaves) are modulated to encode information as though it were a normal radio transmitter. Thus, things turn full circle, for the original microwave oven was based on the magnetron from a military radar. From conflict to domesticity to conflict, then, in a mere six decades.

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Blood transfusion

Painted out

How to disguise red blood cells so that their blood group is invisible



Any colour as long as it's red

THERE are 29 possible combinations of human blood groups, and for a patient to be given a safe transfusion the right one needs to be available. Besides the familiar ABO and rhesus systems, science has (after a sticky start, see article) uncovered the MNS system, the Kell system, the Lewis system and the D+ and D- group. Choose wrong-or settle for a less than perfect match because no other is to hand-and antibodies produced by the recipient's immune system may attack the foreign cells. That can lead to serious consequences. In the worst cases a patient's organs may fail and he may die.

Several attempts have been made to create artificial blood from chemicals that readily dissolve and transport oxygen, or to process the natural stuff in ways that eliminate the antigenic proteins which provoke this immune response. None, so far, has succeeded. But that has not stopped people trying. The latest effort, reported in *Biomacromolecules* by Maryam Tabrizian of McGill University in Montreal and her colleagues, follows the second approach, but with a twist. Instead of purging the antigenic proteins from red blood cells, Dr Tabrizian covers them up.

In essence, what she is doing is painting the cells. And, like all good decorators, she uses two coats. The first-the undercoat-is a material that sticks both to the fatty surface membrane of the red cells and to the mixture Dr Tabrizian chose as the outer coat. Crucially, this second mixture is of no interest whatsoever to the immune system. Nor is anything buried beneath it. Like blemishes on a bathroom wall, the antigenic proteins become invisible when painted over.

In practice, as is often the case when decorating a house, more than two coats may be needed to cover things up. But the layers can be alternated to any thickness desired, and inconvenient antigens thus hidden from view.

And it seems to work. When Dr Tabrizian exposed the newly coated blood cells to antibodies that would normally have been expected to stick to them and cause them to gather in useless clumps, nothing happened. Nor does the coating appear to harm the cells. That is mainly because red blood cells do very little other than absorbing and releasing oxygen and carbon dioxide as appropriate. They have no nuclei and no metabolism worth speaking of, so there is little to go wrong.

Both types of paint are, though, permeable by oxygen and carbon dioxide, and that permeability means the red blood cells can still do their job. Initial tests monitoring the flow of oxygen in and out of the cells show that they are able to transfer the gas just as efficiently as cells that have not been tampered with.

What Dr Tabrizian and her colleagues have not yet done is put their new creation back in an animal. That is the next test. But if the cells do work *in vivo* as well as *in vitro*, the team will have taken a big step on the road to the much-desired goal of blood transfusion that no longer has to worry about matching blood groups.

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Planetary exploration

Mercury rising

The latest mission to Mercury will map an enigmatic planet in detail



EVEN by the standards of space travel, it has been a long, strange trip. But now it should be over. If all went according to plan, at one o'clock in the morning of March 18th-shortly after *The Economist* went to press-*Messenger* will have settled into orbit around Mercury, the planet closest to the sun. It is the end of a journey that has taken the craft, launched in 2004 by NASA, America's space agency, past Earth once, Venus twice and Mercury itself three times already. It is also the beginning of an intense scrutiny of the tiny world, which has otherwise remained unvisited by spacecraft since *Mariner 10* zoomed past it in the 1970s.

The trip has taken so long because exploring the inner solar system is a tricky business. Gravity accelerates spacecraft as they fall towards the sun. Without its six fly-bys-which used the gravitational fields of the planets involved to counter that effect-*Messenger* could not have slowed sufficiently to allow it to drop into its intended orbit. Despite the difficulty of getting there, though, Mercury is a juicy target. Since the great reclassification of astronomical objects in 2006, which saw Pluto lose its planetary status, Mercury has been listed as the smallest planet in the solar system. It is also the second densest, has the oldest planetary surface (parts of which seem to date back almost to the formation of the solar system, 4.5 billion years ago) and experiences the most dramatic daily temperature fluctuations. The mercury, as it were, can hit 400Âº C when the sun is above the horizon, yet dips below -150Âº C at night.

Messenger has already revealed plenty of tantalising information. *Mariner 10* managed to map about 45% of Mercury's surface as it sped past, but *Messenger*'s three fly-bys have filled in the gaps, and there is now a virtually complete map of the place. The surface is a jumble of craters, plains and immense, cliff-like scarps that can be hundreds of kilometres long. Astrogeologists suspect these scarps may be analogous to the wrinkles on a raisin, having formed billions of years ago as the planet's surface cooled and shrank.

Indeed, the more that is learnt about Mercury, the more intriguing it becomes. Its density is presumed to indicate a metallic core, probably made mostly of iron. No other explanation is plausible. That core, calculation suggests, takes up around 60% of the planet's volume, making it far larger than the cores of Venus, Earth and Mars, the solar system's other rocky planets. How this has come about is the subject of intense speculation, with three theories jostling for the top spot. Two of these theories hold that Mercury used to be much bigger. Either it was then hit by an asteroid which blasted much of its surface into space, or else the hot, young sun simply vaporised its outer layers. The third theory argues that drag in the dusty nebula from which the solar system formed would have herded the heavier, metal-rich bits of dust in that nebula into orbits close to the sun, and that Mercury eventually condensed from these. Each theory predicts a different mixture of surface rocks. *Messenger*'s instruments should help settle the question and shed more light on the early history of the solar system.

There are other mysteries. Neither Mars nor Venus has a magnetic field like the Earth's, which is generated by currents in the planet's molten core. But Mercury does. This field was discovered by *Mariner 10*. That it was like the Earth's was confirmed in 2008 on one of *Messenger*'s fly-bys. In orbit, the probe will be able to study the field in detail, which should reveal more about Mercury's structure and may suggest how the core has managed to remain molten over the billions of years since the tiny planet was formed. It will also follow up radar data from Earth-based telescopes, which suggest that there may be ice at the planet's poles, locked away from the scorching sun in the bottoms of ancient craters-as is also believed to be the case on the moon.

A long to-do list, then. Yet all this attention serves only to show how hard exploring Mercury is. The moon, Mars, Venus, two asteroids and even one of the moons of Saturn have all received the attentions of landing craft. The surface of Mercury, too, was to have been visited in 2020, courtesy of a joint European and Japanese mission called BepiColombo. But that landing was cancelled in 2004, though two orbiters should still make the journey. So, despite all the fresh attention *Messenger* will give it, Mercury will remain the least-explored of the inner planets for some time yet.

Climate change and crop yields

One degree over

Data from crop trials underline the threat climate change poses to farmers



As high as an elephant's eye?

FOR a scientist, there are few happier accidents than finding a trove of data that were gathered for other purposes, but which apply to your pet problem. That happened to David Lobell, a researcher at Stanford University, when he started talking to Marianne BÃ¤nziger of the International Maize and Wheat Improvement Centre, in Mexico, about how climate change would affect crops in Africa.

Dr BÃ¤nziger and her colleagues had been running an ambitious set of field trials designed to look at what sorts of maize (corn, to Americans) grow best in various parts of southern and eastern Africa, paying special attention to drought resistance. They were struggling, though, to find the money to pull the results from 123 separate research stations together into one big, tractable database. Dr Lobell realised that if he helped them he could also use the result to correlate yields with meteorological conditions other than drought, and thus reveal any harm done by hotter-than-usual weather. His conclusions, published this week in *Nature Climate Change*, confirm for the tropics the findings for temperate climes of a recent American study. This is that peak, rather than average, temperatures are what matter most to maize.

Days above 30^C are particularly damaging. In otherwise normal conditions, every day the temperature is over this threshold diminishes yields by at least 1%. Moreover, days where the temperature exceeds 32^C do twice the harm of those at 31^C. And during a drought, things are worse still. Then, yields take a hit of 1.7% per day over 30^C.

This matters because increasing the average temperature only a bit can multiply the number of the hottest days a lot. The research predicts that a 1^C rise in average temperature will reduce yields across two-thirds of the maize-growing region of Africa, even in the absence of drought. Add drought and that effect spreads over the entire area.

There is one caveat. Using data from crop trials risks exaggerating the problem, because the plants in such trials are usually well fertilised-unlike most normal maize planted in Africa. Underfertilised crops have lower average yields to start with (which is why encouraging appropriate fertiliser use is important in Africa), but they tend not to be as badly hit by heat and drought as well-fertilised ones. However, the new results accord with one of Dr Lobell's previous studies, which was based on actual harvest data rather than crop trials and suggested yield losses of 20% or more for African maize by the middle of the century.

Perhaps more important than the specific results, though, is the insight that data from crop trials could be used to look at the effects of warming on other farms in other places. Dr BÃ¤nziger says she is now planning to move on to wheat, which is widely seen as even more climate-sensitive than maize. There are nowhere near enough data available on climate and farming in the poor world. To find a previously untapped supply is worth celebrating, even when the news is bad.

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Imperial Chinese porcelain

Meiyintang marvels

The finest private collection of Chinese porcelain in the West is about to be sold



ON APRIL 7th, as part of its spring season in Hong Kong, Sotheby's will be selling 77 lots of imperial Chinese porcelain from the Meiyintang collection. The announcement, made last month on the day that the auction house held a record-breaking modernist art sale in London, has attracted little public attention. But to those who follow the market in Chinese artworks, news of the Hong Kong auction was nothing short of a thunderbolt. For Meiyintang is regarded as the greatest collection of Chinese treasures still in private hands in the West, a name ranked alongside Alfred Clark and Sir Percival David, passionate scholars whose collections were among the most important ever made outside the great museums of Beijing and Taipei.

Not so long ago the Chinese were prevented by the Communist Party from celebrating the achievements of their forebears. But with new fortunes being created all the time now in China, dealers and collectors from Hong Kong and the mainland have become enthusiastic buyers. They have a thirst for their own history, especially for anything that connects modern China with the glories of its imperial past. For the first time last year, according to a report released on March 14th, China overtook Britain to become the biggest art market in the world after America.

Demand for Chinese artworks has driven up prices, which in turn is drawing fresh treasures on to the market. The traffic is almost entirely one way. Chinese fine art from America and Europe is moving back to China in the biggest migration of culture since European masterpieces travelled inexorably westward to America in the 19th century. Buyers prize rarity, quality and provenance above all.

The Meiyintang collection will generate considerable Chinese interest because of its quality and the secrecy surrounding its creation. Despite its fame, the 2,000-piece collection has rarely been seen in its entirety, and then only in private. A few works were exhibited at the British Museum in 1994 and in Monte Carlo two years later. The only public record is a monumental catalogue by a German scholar, Regina Krahl. Though it runs to seven volumes, the catalogue says nothing about who put the collection together.

Sotheby's, Ms Krahl and Giuseppe Eskenazi, the London-based dealer who serves as Meiyintang's chief adviser, refuse to identify those behind it. But *The Economist* has learned that the guiding hand is that of a 93-year-old Swiss businessman, Stephen Zuellig. Born in the Philippines, Mr Zuellig and his younger brother, Gilbert, who died in 2009, spent 60 years building up their father's small Manila-based trading house. Today the Zuellig Group is a leading provider of health-care services and pharmaceuticals in Asia and one of the region's biggest agribusinesses, with an annual turnover of around $12 billion. The group, which is still largely owned by the family, has created a sizeable fortune for the brothers.

The Zuelligs began buying Chinese artworks in the early 1950s through Helen Ling, the American wife of their Singapore associate, who traded Chinese porcelain in Shanghai. It was she who introduced them to Edward Chow, the dominant Chinese collector-dealer of the post-war years who was based in Hong Kong and later in Switzerland. From an early stage the brothers were interested in the whole range of Chinese art, from archaic bronzes to late imperial porcelain. But they divided their specialities by date: Gilbert focused on early ceramics from the Neolithic period to the Song dynasty and Stephen the porcelain of the Yuan, Ming and Qing dynasties.

They chose the name Meiyintang, which means "hall among rosebeds" in Mandarin, but it is also a play on the Meienberg at Rapperswil, the Swiss estate south-east of Zurich that their grandfather bought in 1912, where both brothers maintained a home and where Stephen Zuellig displays his treasures in a long underground gallery.

The Zuelligs sought out the best specialist dealers, among them Priestley and Ferraro for early works. Mr Eskenazi focused on the later periods and, over a quarter-century, sold them (or acquired on their behalf) more than 160 pieces. But it was Chow, a collector who inspired affection combined with a degree of awe, who influenced the Zuelligs the most.

Three fundamental criteria guided their buying: a work's rarity, the quality of its decoration and the condition of the piece. As a general rule, particularly with the Qing dynasty treasures, complex three- dimensional pieces, such as vases, took precedence over more utilitarian cups and bowls, with flat plates being the least important and least desirable objects. The Zuelligs were, of course, not the only collectors to apply these general principles, but they are said to have been particularly rigorous in applying them. It was not enough that a work should be rare or important; each piece they bought also had to have a personal aesthetic appeal. "They bought as much with the heart as the head," says Nicolas Chow, the Sotheby's director in charge of the sale, who happens also to be Edward Chow's grandson.

Next month's auction is expected to be the first of several which will concentrate, at least for the moment, on the Yuan, Ming and Qing ware collected by Stephen Zuellig. In picking out what to include in this initial sale, Mr Zuellig has chosen pieces that represent a microcosm of the entire collection, ranging from the Yuan dynasty that began in the late 13th century to the glories of Emperor Qianlong's reign and that of his son, Jiaqing, who died in 1820.

Most important are the cobalt-blue and copper-red early Ming wares that are decorated under the glaze, the monochrome Ming and Qing pieces, and early Qing enamelled porcelain whether *famille-verte* or *famille-rose*. Many of the works are unique. When Mr Eskenazi held an exhibition of seven Qing dynasty "peachbloom" vessels in 2006, Mr Zuellig bought the two rarest pieces, a waterpot and a "three-string vase". He already had examples of the others. The Meiyintang group (pictured above) is estimated to sell next month for HK$50m-70m ($6.4m-9m). Mr Zuellig's blue-and-white Chenghua "palace bowl" may have a plain white interior, but the exterior decoration, with its large clusters of melon vine, all painted in a watery blue and each subtly different, is Chenghua painting at its best. Little surprise that Sotheby's estimates the bowl will sell for HK$80m-120m.

Similarly, the eight-inch (20cm) vase painted with pheasants looks ordinary enough until you compare it with others of a similar kind. Each example is different, but only in Mr Zuellig's pheasant vase do you see the combination of creamy glaze, the birds positioned looking away from one another and yet very much part of a whole landscape, and the subtle colouring as if the painting had been done on silk rather than porcelain. Bought in Hong Kong at the height of the Asian

crisis in 1997 for HK$9.9m, then a record for Qing porcelain, the Meiyintang pheasant vase is now estimated to fetch HK$180m-300m.

Every major auction starts a new collection. With rare exceptions, Chinese purchasing over the past decade has been a case of buying what is fashionable and expensive rather than collecting out of aesthetic passion and scholarly knowledge. The Zuelligs' Meiyintang porcelain is very much a European collection of a particular taste. China has some extraordinary museums, but no old collectors for the new buyers to emulate. That will change with time, and the new private collections in China may soon be as unique in their way as the Meiyintang is now.

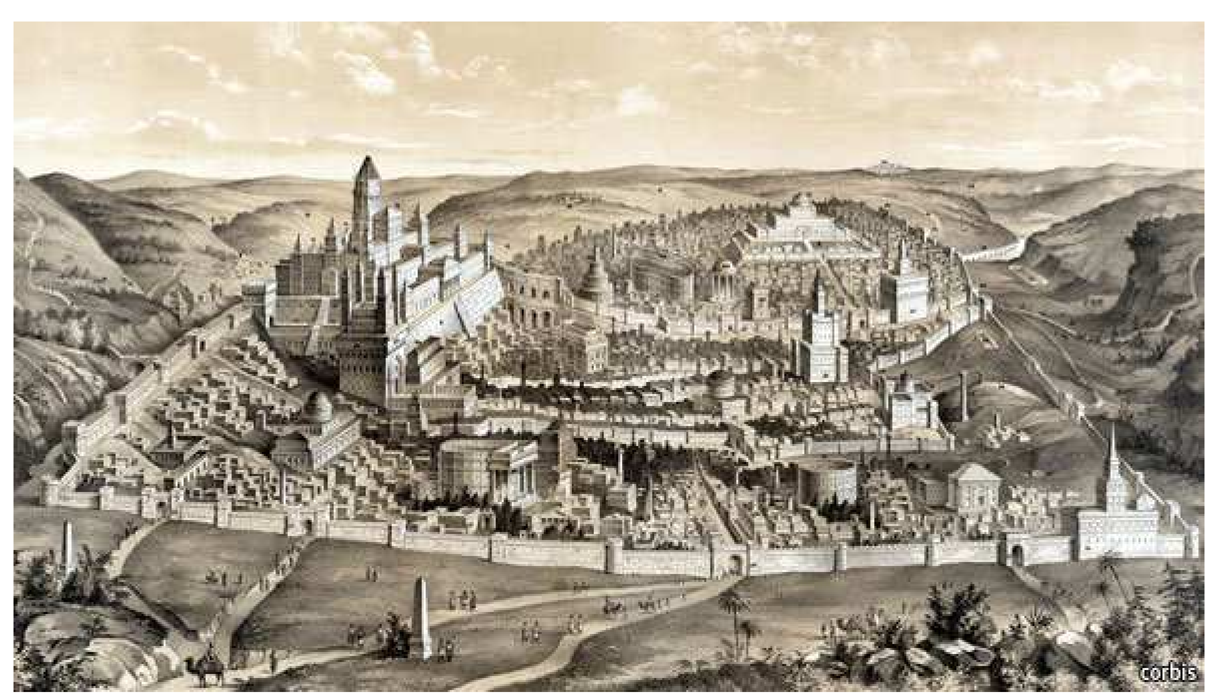
Jerusalem

City on the hill

The prize of empire builders and the seat of quarrels

Jerusalem: The Biography. By Simon Sebag Montefiore. *Weidenfeld & Nicolson; 638 pages; pound25. To be published in America by Knopf in October; $35.* Buy from Amazon.com, Amazon.co.uk

Jerusalem, Jerusalem: How the Ancient City Ignited Our Modern World. By James Carroll. *Houghton Mifflin Harcourt; 418 pages; $28.* Buy from Amazon.com



And there Jerusalem's pillars stood

IT TAKES almost 100 pages for Simon Sebag Montefiore's magisterial biography of Jerusalem to come to Jesus Christ. By that time the city had been fought over by Babylonians, Israelites, Jews, Philistines, Jebusites, Assyrians, Persians, Greeks, Macedonians, Maccabees, Romans and Herod and his descendants. Jerusalem was, as Mr Montefiore says, a veritable "tower of Babel in fancy dress".

The prize of empire-builders through the ages, Jerusalem had been dashed time and time again to the ground, only to rise up anew-physically, politically, even spiritually. At the time of Christ's birth it was already the shrine of one faith and about to become that of a second; half a millennium later the Muslims would claim it as the shrine of a third. It is the site of the Judgment Day. Unlike anywhere else it exists in two places at once; on earth and in heaven. No other city, not even Athens in ancient times, has been fought over so much as Jerusalem.

Mr Montefiore is related to Sir Moses Montefiore, an Italian-born British Jew (described by Lord Shaftesbury as "that grand old Hebrew") who was knighted by Queen Victoria and became the first European to be allowed by the Ottomans to visit the Temple Mount in Jerusalem in 1855. Known for his early work on Josef Stalin and Catherine the Great, Mr Montefiore, now 45, has, nonetheless, been preparing all his life to write this particular book. And he has given much thought to how it should be approached.

The story of Jerusalem is told chronologically through the lives of the men and women-prophets, poets, peasants and soldiers, kings and conquerors-who shaped it. Among the thousands of books on Jerusalem very few are narrative histories, and this straightforward approach works well. Mr Montefiore steers a clear path through the religious animosities and political intrigues that continue to this day, adopting a strikingly apolitical tone.

He adds richness by including sources not usually available in English. One example is the diary of Wasif Jawhariyyeh, an Orthodox Christian who studied the Koran. Born at the tail end of the 19th century and steeped in the cosmopolitanism of Jerusalem, Jawhariyyeh displayed an early gift for the lute or *oud*, which, in a city that loved music, gave him access to everyone high and low. His lyrical account of Jerusalem life over 40 years is astonishingly still only available in Arabic, but the author had it translated and makes good use of Jawhariyyeh's material.

As a writer, Mr Montefiore has an elegant turn of phrase and an unerring ear for the anecdote that will cut to the heart of a story. When Queen Victoria's son, the 20-year-old Prince of Wales and future King Edward VII, rode into Jerusalem in 1862, escorted by 100 Ottoman cavalrymen, the plump princeling could think of little else but getting a Crusader tattoo on his arm; when Hussein, the Sherif of Sherifs, became Emir of Mecca in 1908, his telephone number was Mecca 1. It is this kind of detail that makes "Jerusalem" a particular joy to read.

Mr Montefiore's chronicle stops in 1967, when the Six-Day War saw Jerusalem divided between the Arabs and the Israelis, a cut-off date that allows him neatly to sidestep the consuming quarrel of our age. James Carroll, by contrast, has no such qualms. His history also begins in ancient times and he goes on to analyse the importance of the Crusades. However, his modern focus is on the tension between Christian Jerusalem, Jewish Jerusalem and Islamic Jerusalem, between Israeli Jerusalem and Palestinian Jerusalem, and how the bible-based myth of Jerusalem shaped new-world thinking, from Governor Winthrop to Abraham Lincoln, Woodrow Wilson and Ronald Reagan.

"Jerusalem fever", inextricably tied to Christian fervour is, he says, the "deadly, unnamed third party to the Israeli-Palestinian wars." Some readers will balk at the leaps Mr Carroll takes to link American religiosity to Islamic terrorism and the inevitability of nuclear war, but he explains why some Americans support Israel so fiercely. The full restoration of Eretz Israel, the biblical land, with Jerusalem at its centre, will, according to the Book of Revelations, hasten the return of the Messiah. Mr Carroll's book is a far more frightening work than Mr Montefiore's, but they are well worth reading together.

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Computer games

Super Mario management

They really make people smarter

Reality Is Broken: Why Games Make Us Better and How They Can Change the World. By Jane McGonigal. *Penguin Press; 388 pages; $26.95. Jonathan Cape; pound12.99.* Buy from Amazon.com, Amazon.co.uk

WITH the exception of group sex and trainspotting, few pastimes get a worse press than computer games. The stereotypical gamer is a fat bachelor in a darkened bedroom, living on pizza and substituting pixels and joysticks for healthy human contact.

Jane McGonigal, a computer-game designer, is keen to change this view. Games, she says, are increasingly played with others rather than alone. They help fulfil human needs. Simple online games such as Lexulous, a Scrabble clone played

between friends on Facebook, can help sate the desire for companionship among atomised young people. Collaborative multiplayer games cater to the need to feel part of a group. Others play up the sense of skill and mastery that comes from overcoming a particularly fiendish challenge, or even provide their players with the need for hard, rewarding work.

But Ms McGonigal aims to do more than to calm a moral panic. She believes that games-or the lessons learned by those who design them-hold important lessons for life in the real world.

The most persuasive example concerns World of Warcraft, an online, multiplayer, swords-and-sorcery game played by some 11m people worldwide. The game revolves around making your character more and more powerful, in large part by completing an almost endless series of missions, either alone or as part of a closely co-ordinated group.

Players and critics alike have noted the game's resemblance to a job, and a fairly menial job at that. And yet, thanks to a mixture of the social interaction offered by the game and a steady stream of shiny (and entirely virtual) rewards that help to foster a powerful feeling of productivity, people spend about 30m man-hours every day toiling inside the World of Warcraft, at a cost to each player of about $10 a month.

To many, that alone is a symptom of addiction. But Ms McGonigal sees instead a keen understanding of applied psychology and an expert ability to motivate people. Computer games, she says, feel in many ways more rewarding than the real world; the tasks are clearer and more manageable, feedback is instantaneous and rewards (which are entirely virtual, and thus free to manufacture) are quick and plentiful. Management consultants, who have long pondered the question of how to motivate workers, could do worse than study how Blizzard Entertainment, which develops World of Warcraft, keeps its game players happy and productive.

Traditionalists may scoff. But reality is already beginning to learn from its virtual counterpart. Lessons from game design have been used by Nike to encourage people to get fit, by the *Guardian* newspaper to enlist the help of its readers in digging through the WikiLeaks cables, and even by a school in America to help motivate its pupils. Frustratingly, few of the book's other examples are as thought-provoking or as convincingly argued as World of Warcraft. Occasionally, Ms McGonigal lapses into fantasy: even given the well-known eccentricities of the awarding committee, it will probably be a long while before a game designer wins the Nobel peace prize. And the frequent mentions of her own games lends the book an unwelcome air of self-promotion. Still, her central idea-that games hold lessons for the real world as well as vice versa-is interesting, and worth taking seriously.

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New fiction from Sudan

Desert rose

A novel of changing times

Lyrics Alley: A Novel. By Leila Aboulela. *Grove Press; 310 pages; $24. Weidenfeld & Nicolson; pound18.99.* Buy from Amazon.com, Amazon.co.uk



LEILA ABOULELA'S "Lyrics Alley", which has been shortlisted for the 2011 Orange prize for fiction, is set in Sudan, as it sloughs off British and Egyptian rule and prepares for its new liberty. Mahmoud, the urbane patriarch, straddles two worlds, embodied in his two wives. The first, Waheeba, is Sudanese; her bulk swathed in a traditional tobe, the tribal scars on her face like "cracks on a French loaf". Spoilt Nabilah, his younger second wife, is an Egyptian glamourpuss, who sulkily divides her time between Egypt and Sudan, infuriated at the "primitiveness" of her new home, sullen at the heat and squalor of her husband's "untamed land". Dismissive of Waheeba, she scorns the very idea that this lump of a woman, "obese, menopausal, illiterate", could be her rival in anything.

Different as they are, Mahmoud "glides gracefully" between his two worlds, enjoying both Cairo's avenues and the alleys of Umdurman. But when Nur, his beloved son, is paralysed after a diving accident on holiday in Alexandria, the balance is upset. Their lives falter. The once stable trio of Waheeba, Nabilah and Mahmoud is rocked.

Lying in bed, Nur's paralysis crushes him like a giant thumb, "meaty and human, grotesque with a brittle purple nail", pinning him down. He is consumed by anger, "solid and opaque". But then, amid the turmoil, Nur finds solace writing poetry: odes to his homeland and his lost love. He hones his skill like a fisherman, learning to cast his net "into a river of dreams and catch a splendid array of words."

Politics inevitably steals into Nur's verses, mixed with his own suffering: "In you, Egypt, are the causes of my injury. And in Sudan, my burden and solace." Ms Aboulela paints the history that unfolds behind the family upheaval with a delicate hand. There are moments of drama-a demonstration at the university, a parade-but these are rare. Instead she offers characters that absorb and fascinate. None is without redeeming features; Nabilah's gentle love for her grandmother tempers her petulance; boozed-up Nassir, Nur's brother, buys glasses for Soraya, his bookish but myopic cousin, in defiance of his elders.

Particularly well-drawn is the battle over whether to circumcise the family's daughters. Mahmoud, supported by Nabilah, is implacably opposed. Waheeba, desperate for her daughter to fit in to Sudanese society and anxious that no man will want to marry her, circumcises her in secret. Resentful of her rival, she has Nabilah's daughter circumcised too. There are metaphors in this episode for Sudan's struggle to find its new identity, the tug between the old ways and the new. But its power lies in its depiction of humanity; the anguished rage of a mother at what has been done to her daughter, the vindictive envy of the old wife passed over for the new, a child's bewildered pain and fear.

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The history of transfusion

Bloody victory

The evolution of a science

Blood Work: A Tale of Medicine and Murder in the Scientific Revolution. By Holly Tucker. *W.W. Norton; 288 pages; $25.95.* Buy from Amazon.com



Blood and guts

MILLIONS of blood transfusions are performed each year, saving countless lives. Yet, this was once a controversial procedure. Shortly after the first experiments were conducted in England and France some 350 years ago, blood transfusion was banned by the French parliament, effectively halting all such trials in Europe. Almost 150 years passed before the practice was revived in 1818 by an English obstetrician, James Blundell, who performed a human-to-human blood transfusion at Guy's Hospital in London. Even then, transfusion was only occasionally successful. It was only after the discovery of blood groups and anticoagulants in the 20th century that it became a common medical procedure.

The controversy that led to the French ban is central to Holly Tucker's excellent book. On June 15th 1667 a young French physician, Jean Denis, successfully transfused a few ounces of blood from a lamb into a 15-year-old boy in the first animal-to-human transfusion. The boy lived. Two years earlier, in England another physician, Richard Lower, had already successfully transfused blood between dogs.

Denis, who came from a humble background and was considered an upstart by the Parisian medical establishment, wanted to make a name for himself by extending the English experiments. In December 1667, six months after he injected lamb's blood into his teenage patient, he made two separate transfusions of a calf's blood into Antoine Mauroy, a notorious madman in Paris. Mauroy died within a few weeks, and Denis soon found himself accused of murder.

Denis's experiments had pitted him against the medical and religious conservatives of the day, who believed that the blood was the seat of the soul, and flowed from the liver to the heart, as the Greek physician Galen had maintained in the second century. Transfusion was regarded as a form of blasphemy, to be avoided at all costs. When Mauroy died, Guillaume Lamy, one of the doctors opposed to Denis's experiments, rejoiced that "the madman's death will be enough to overturn all of his beautiful imaginations and to ruin entirely his high hopes." What followed is a classic tale of power and intrigue, a "blood war" which Denis lost.

Ms Tucker's chronicle of the world of 17th-century science in London and Paris is fascinating. A meticulous historian, she paints a compelling picture of rivalries and politics among the various English and French academies and their members. In an interesting twist, she even unearths evidence that Mauroy died, not as a result of the transfusion, but because he was murdered by Denis's opponents.

The author also highlights the messy way scientific revolution takes place, and not just in the 17th century. With the current stem-cell controversy in mind, Ms Tucker says: "Every era must necessarily confront some of the same time-worn

debates about whether the contours of the human body, mind and soul are as stable as we might like them to be." Some of the sentiments that surrounded the blood wars of the 1600s still haunt medical research today.

Stories from Croatia

Animal farm

The tale of the mouse and the mole

A Guided Tour Through the Museum of Communism: Fables from a Mouse, a Parrot, a Bear, a Cat, a Mole, a Pig, a Dog & a Raven. By Slavenka Drakulic. *Penguin; 192 pages; $14.* Buy from Amazon.com

MANY, many generations ago there stood a massive concrete structure called the Berlin Wall. The wall fell in 1989; not so far back if you are human, but if you are a mole, a very, very long time ago.

After 20 years what more could there be left to say? Slavenka Drakulic, a well-known Croatian author, has one answer: communism through the eyes of animals. She succeeds with a flair for observation, gossip and history. The result is a jolly good read.

Lecturing to a learned society of Berlin moles, the hero recounts the story of the people who tunnelled to get from one side of the wall to the bit of Berlin in the middle, which was surrounded. Here were bananas as good as the juiciest earthworms. However, a desire for bananas was "only one aspect of it". In one part of the Overland, the mole explains, religion was all but forbidden, but in the other there were huge churches "called shopping malls".

A dog says that the wild dogs that roam Bucharest today are the great-great-grandchildren of those set loose when Nicolae Ceausescu obliterated the historic city centre to build his own grandiose creations. It is tough being an old dog, says canine Karl, echoing an oft-heard nostalgia expressed by human Romanians. Before, all dogs worked, guarding homes and providing comfort. What is missing today, he says, is security.

From Bulgaria Tosho reminisces about his time as a Roma's dancing bear. How could bears undergo "torture without even a squeak"? Well, he growls, at the time it was not just your body which was captured, but your mind too. No one rebelled, "because the thought never occurred to us."

The strongest story comes from Koki, a Croatian parrot, who in exchange for nuts reminisces about Marshall Tito's jealous wife and his curvy masseuses. But the parrot has serious things to say too. Tito made 20m Yugoslavs believe they were free. "Well, their cage was more colourful than others of their kind, but it was still a cage. Yet people believed him, as did Koki-birdie, too." Ms Drakulic's words are not easily forgotten.

Simon van der Meer

Simon van der Meer, tamer of subatomic particles, died on March 4th, aged 85



SUBATOMIC particles can be wayward. Getting them to behave in huge circular accelerators like the Large Hadron Collider is fiddly. But Simon van der Meer had a knack for that. He was a natural tinkerer, fascinated by how machines worked and how they could be made to work better. In 1940, as a teenager in The Hague under Nazi occupation, he cobbled together scavenged parts to make simple radios and, as he modestly put it, "equipped the parental home with various gadgets". Such a talent for fiddling was just what CERN needed.

Europe's main nuclear-research institute, which sits on the Franco-Swiss border near Geneva, poached Mr van der Meer from Philips, a Dutch engineering giant, in 1956. The laboratory had been set up two years earlier to revive European fundamental physics after the war. Mr van der Meer's first job was to tinker with the power converters that delivered electricity to the institute's accelerators. That sparked his interest in accelerators themselves. In the early 1980s he was still busy, but with a much grander brief.

By then CERN was in a race to justify its existence. The laboratory could boast just one ground-breaking result since it had set up shop: the detection in 1973 of neutral currents, which provided the first inkling of the electroweak theory that unified electromagnetism and the weak nuclear interaction, two of the four fundamental forces of nature, in one elegant mathematical framework. And even that was no more than a partial success. The theory's vindication would come only with a glimpse of W and Z bosons-particles which, it posited, carried the weak force, just as photons carried the electromagnetic one.

The rub was that both W and Z are heavy. According to Albert Einstein's famous equation, $E=mc2$, the heavier the particle, the more energy is needed to produce it. In the 1970s accelerators were capable of ramping up the speed and thus the energy of particles, but could only smash them into a stationary target. Mr van der Meer wanted to get particles to hurtle into each other head on.

An idea was being floated to use protons and their antimatter equivalents to do just that. Since matter and antimatter are identical in all but charge, they could, in principle, be accelerated in opposite directions by the same set of magnets, in the same ring, at the same time-ingenious, and cheap. But there was a catch. The two sorts of particle would both have to travel in tightly packed beams. Too diffuse a beam, and they would miss each other by the subatomic equivalent of a mile.

For years on end Mr van der Meer made a study of the statistical properties of the motion of particles in accelerators: sometimes late into the night, and sometimes lost in deep reflection. By 1968 he had concluded that they could be kept in order by stochastic (ie, random) cooling: identifying a wayward particle on one side of the accelerator ring, sending a signal directly across to the other end, and tweaking the magnetic field to nudge the oncoming errant particle back into the beam.

But could it be made to work in practice? For a long time, he thought not. He shelved the idea as "too far-fetched" until, in 1972, a colleague pushed him to revisit and publish it. Even then, he doubted that it would be any use to anyone: but still, his paper concluded, "it seems useful now to present at least some quantitative estimation of the effect." Two years later it was tested, and it worked.

By 1976 the drive to convert CERN's new accelerator into a proton-antiproton collider was on, spearheaded by Carlo Rubbia, an Italian experimental physicist. Mr Rubbia was as garrulous and extrovert as Mr van der Meer was quiet; a typical duo of sober engineer and crazy physics man. Yet quietness prevailed when Mr van der Meer announced one morning: "I can do everything with stochastic cooling," and Mr Rubbia had to agree.

In 1978 the project got the go-ahead; the protons and antiprotons, neatly marshalled, collided, and in January 1983 the team announced the first sightings of W. They made the front page of the *New York Times*. Those of Z were made public later that year. It was, said the *CERN Courier*, "one of the great milestones in man's quest to understand the Universe around him." In 1984 Mr van der Meer shared the Nobel prize for physics with Mr Rubbia. He went up modestly behind his colleague.

Slightly amateur

He became only the second accelerator engineer to be recognised by the Swedish Academy. Yet he was also a physicist, lingering at CERN, which he found "agreeable and stimulating", until his retirement in 1990. He was always aware, and often sorry, that his degree from Delft University of Technology was in technical physics, and that the pure science he learned in that venerable engineering school was "of necessity somewhat restricted". But he would comfort himself that his "slightly amateur" approach to pure physics made him look at problems in a different way.

That difference was essential. In the end, physics is an empirical science. It needs clever experiments; and such experiments need nifty devices. Without them, many beautiful theories would be merely that-beautiful. It is only thanks to tinkerers like Simon van der Meer that some of them also turn out to be true.
